FILED
991367 FEB 14 2000
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No. 99-

IN THE

Supreme Court of the United States

AMILIA ABBOTT, *et al.*,

Petitioners,

v.

MEDGAR EVERS HOUSES ASSOCIATES, L.P., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

In a civil RICO action based on predicate acts of mail and wire fraud,

1. Should the rule for pleading proximate cause incorporate the controversial "convergence theory" and require that the plaintiff must have received and relied upon the fraudulent mailings and wirings, as held by the Second and Fourth Circuits, or that the plaintiff need not have received and relied upon these mailings and wirings, provided that they directly caused plaintiff's injury, as held by the Third and Fifth Circuits?

2. Did the Court below ignore this Court's holding in *Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258 (1992), by creating a black-letter rule that an injury to a plaintiff caused by misrepresentations to a third party is "necessarily derivative" of injuries sustained by the third party?

3. Did the Court below improperly engraft the element of justifiable reliance onto petitioners' cause of action, contradicting this Court's holding in the criminal context that "justifiable reliance . . . plainly [has] no place in the federal fraud statutes," in *Neder v. United States*, 527 U.S. 1, 119 S. Ct. 1827, 1841 (1999)?

LIST OF PARTIES

The names of all parties in the court whose judgment is sought to be reviewed appear below:

Petitioners:

Amilia Abbott, Kanvra Abdul-Karim; Edwin Acervedo; Carolyn Adams; Deborah Alston; Patricia Alston; Marlene Anaya; Annie Barnes; Charise Barnes; Sheila Batts; Jeanine Bell; Cecilia Benique; Clinton Biet; Teresita Bowman; Elizabeth Browde; Annette Brown; Cora Brown; Jerelyn Brown; Leona Brown; Robert W. Brown; Roberta Brown; Ramona Bryan; Cheryl Burke; Sandra Byrd; Debbie Cannon; Pernice Carroll; Hazel Carter; Marsha Carter; Louise Chaneyfield; Sonia Clintron; Karen Cleveland; Toni Cleveland; Cora Cofield; Belinda Collier; Gwendolyn Cooper; Shirley Cooper; Shirley Corley; Antonia Creel; Deborah Davis; Kim D. Day; Ruby Dicks; Monique Dorsey; Douglas Drayton; Lovellan Dunton; Mary Dyson; Robert Edward; Beatrice Estwick; Kahesa Farmer; Sally Farmer; Margaret Fason; Carmen Feliciano; Sheri-Ann Felix; Paulette Ferguson; Francine Fortune; Latisha Frederick; Dorthy Mae Gainyard; Estelle Gibson; Geraldine Giles; Margaret Gillyard; Ethel Gladden; Modesto Gonzalez; Pamela Gordon; Concencia Gorman; Ernestine Green; Elsie Griffin; Joan Griffith; Sheila Grimes; Remona Hall; Rachel Henderson; Crystal Hollins; Sylvia Holman; Lorena Holme; Gloria Howard; Flora Hudson; Virginia Jackson; Deborah Jones; Ethel Jones; Mattie Jones; Odessa Jones; Gregory Kearse; Gladys Kendrick; Loretta Knox; Ronald Knox; Wanda Knox; Albert Langston; Barbara Lewis; Odessa McKenzie; Jean Mabry; Joseph Maddox; Arlene Madison; Donna Mahon; Darene Mallery; Gloria Marcus; Luz Martinez; Diane Mashburn; Addie Mazyck; Brenda Michel; Joann Mitchell; Theresa Moody; Letona Moffett; Willena

Moore; Medgar Evers Houses Tenants Association; Grace Morgan; Rachael Morris; Shalon Murdaugh; Rochelle Murdaugh; Edwina Murphy; Kisha Nelson; John Nixon; Lee Anne Ogbewele; Cheryl L. Page; Barbara Paign; Vonzella Palmer; Vickie Parker; Gale Patterson; Jean Penn; Rosetta Pattiford; Minnie Pierce; Essie Porter; Emma Pratt; Ronnie Pullian; Thelma Pullian; Bettie Ramizee; Carol Reddick; Raquel Rivera; Fdella Robinson; Idela Robinson; Charlotte Rodgers; Lola Rodgers; Linda Roy; Marsha Roy; Jessie Sanders; Lena Settles; Latoya Shannon; Mary Shipman; Theodore Simmons; Sylvia Simpkins; Carrie Simpson; Onella Simpson; Hazel Smalls; Sharron Smith; Sonia Smith; Latisha Spencer; Picola Spencer; Janice Staton; Jocynthia Stokes; Johnie Stovall; Carol Sutton; Evelyn Sutton; Alison Taylor; Maxine Taylor; Chester Thomas; Karen Thomas; Laraine M. Thomas; Monica Thomas; Shirley Thomas; Shana Thompson; Tenyatta Turpin Gregory; Aisha Tyler; Beverly Vaden; Virginia Vaughan; Gladys Vice; Clarice Wade; June Wallace; Sonia Wallace; Patricia Washington; Alissa Webb; Dorothy White; Banquetta Whitt; Michele Wike; Kathleen Wildmon; Dorothy Williams; Lavon Williams; Michelle T. Williams; Sarah Williamson; Nacomis Wilson; Cassandra Womack; Bonnie Worley; Evelyn Worrell; Darlene Wortham; Ethel Wright; and Tywanna Wright Gardner.

Respondents:

Medgar Evers Houses Associates, L.P.; Philip Rosenberg; Douglas Rosenberg; BPC Management Corp.; Seymour Maslow; Richard Curtis; New England Management Co., Inc.; United States Department of Housing and Urban Development; New York City Department of Housing Preservation and Development.

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PRELIMINARY STATEMENT

Petitioners Amilia Abbott and 180 other tenants of Medgar Evers Houses, a housing project composed of nine buildings located at 590, 600, 620, 630, 701, 715, 735, 745 and 755 Gates Avenue, Brooklyn, New York, and the Medgar Evers Houses Tenants Association ("petitioners"), respectfully petition for a writ of *certiorari* to review the judgment of the United States Court of Appeals for the Second Circuit in the above-captioned case.

OPINIONS BELOW

The summary order of the Court of Appeals for the Second Circuit affirming the district court's dismissal of the Complaint is unpublished and is reproduced in the Appendix at App. 1a. The opinion of the district court granting defendants' motion to dismiss the Complaint is published at 25 F. Supp.2d 116 (E.D.N.Y. 1998) and is reproduced at App. 8a.

JURISDICTION

The judgment of the Court of Appeals for the Second Circuit was entered on November 16, 1999. This Court has jurisdiction to review the judgment of the Court of Appeals pursuant to 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS

The statutes involved in the case include:

18 U.S.C. § 1341, reproduced in the Appendix at 33a.
18 U.S.C. § 1343, reproduced in the Appendix at 34a.
18 U.S.C. § 1961(1), reproduced in the Appendix at 28a.
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42 U.S.C. § 1437f, reproduced in the Appendix at 35a.

The regulations involved in the case include:

24 C.F.R. § 886.108(c)(1), reproduced in the Appendix at 37a.
24 C.F.R. § 265.10(a)(2), reproduced in the Appendix at 42a.
24 C.F.R. § 265.10(a)(4), reproduced in the Appendix at 43a.
24 C.F.R. § 200.219, reproduced in the Appendix at 39a.

Other rules involved in the case include:

HUD Handbook, *Occupancy Requirements of Subsidized Multifamily Housing Programs*, Directive No. 4350.3 Chg. 15, § 6-6A, reproduced in the Appendix at 44a.

STATEMENT OF THE CASE

In 1985, Medgar Evers Houses Associates, L.P. ("MEHALP") acquired ownership of a 315-unit housing project, Medgar Evers Houses (the "project") in the Bedford-Stuyvesant neighborhood of Brooklyn, New York. The income generated by this low-income housing project derived from a combination of petitioners' rents and rent subsidies provided through HUD's project-based Section 8 program, 42 U.S.C. § 1437f, a housing entitlement for low income families through which the United States Department of Housing and Urban Renewal ("HUD") makes monthly rent payments on the tenants' behalf to the owners of the project.

Between 1987 and 1996, MEHALP obtained regular increases in rent subsidy based upon its claims that the additional funds were needed to repair and improve the project and maintain federal Housing Quality Standards requiring all units to be "safe, decent and sanitary." These regular increases raised the project's annual income from approximately $1.2 million per year in 1987 to approximately $3.8 million per year in 1996.

From the time it acquired ownership of the project, MEHALP, together with the management companies it controlled -- defendants BPC Corp. and New England Management Co. (the "management companies") -- and the individual defendants associated with those companies, engaged in a long-term fraudulent scheme to loot funds from the project account.[1]

The total income of the project during this decade included not only the millions of rent subsidy dollars paid by HUD under its Housing Assistance Payment ("HAP") contract with the owners, but millions more paid to the defendants by the petitioners as their direct contribution to the total rent.

Under the HAP contract and accompanying regulations, the owners of project-based, Section 8 subsidized projects are obliged to deliver to the tenants living conditions that comply with federal Housing Quality Standards. Thus, the owners must certify to HUD every month that "all inspections have been completed" and the units for which assistance is billed "are safe, decent and sanitary." HUD Handbook, *Occupancy Requirements of Subsidized Multifamily Housing Programs*, Directive No. 4350.3 Chg. 15, § 6-6A. In spite the principal purpose for which all monies paid to the project must be put -- the provision of safe, decent and sanitary living conditions to the tenants, including the petitioners herein -- and, despite the substantial increases in rental income defendants received, by May, 1997 when this action was commenced, the long-term looting of the project's operation and maintenance funds had

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[1] The funds paid by tenants and HUD as rent and rent-subsidy must, by law, be kept in a project account. *See* 24 C.F.R. § 886.108(c)(1). These funds remain the property of the project and money may only be distributed to the owners as profit *provided* that conditions at the project first meet federal Housing Quality Standards.

resulted in 1,595 housing code violations, 1,188 of which were deemed by New York City housing inspectors to be hazardous to the lives, health and/or safety of the residents.

The defendants' long-term looting of the project account depended for its success on a three-pronged scheme of deception. Since one cannot steal what one cannot obtain, the first prong in defendants' scheme was designed to secure actual payment of the hundreds of thousands of subsidy dollars from HUD each month. To this end defendants mailed false certifications to the agency claiming that each unit for which it was seeking a subsidy payment was in safe, decent and sanitary condition. In this way, defendants obtained payment of more than $25,000,000 from HUD by the time this action was commenced.

The second prong of defendants' scheme to engage in the long-term looting of project funds was to prevent, forestall and/or divert any effort by HUD to use its enforcement powers. Those powers include ouster and replacement of management, assumption of mortgagee-in-possession status and, if necessary, foreclosure and recovery of ownership, to secure needed repairs and improvements and remedy deficiencies in the physical conditions and management of the project.

Whenever HUD inspectors did identify conditions in need of repair or correction, the defendants responded with a pattern of false and misleading submissions and promises to HUD regarding not only existing conditions but future plans to improve the property and/or abate violations of federal Housing Quality Standards. Invariably, defendants prepared and transmitted letters and other documents to assure HUD that they were seeking bids or had contracted for work when such work was never planned or implemented. These false

assurances of repair and improvement to the project lulled HUD into foregoing its enforcement responsibilities.

Finally, in order to avoid detection by HUD of their wholesale looting of the project's operation and maintenance funds, the defendants implemented the third prong of their scheme, consisting of the preparation and submission to HUD of dozens of false and misleading monthly and annual financial statements. These statements concealed the massive misappropriation of funds from the project account which were required to be used for the maintenance and operation of the project.

The thirteen-year pattern of mail and wire fraud through which the defendants successfully carried out their scheme to loot the project eluded official detection until the petitioners commenced this action. Following the commencement of this action, the defendants consented to HUD becoming the mortgagee-in-possession of the project and, since June, 1997, HUD has been responsible for its management.

During the thirteen-year period prior to the commencement of this action conditions at the project steadily deteriorated. Because of the relentless looting of the project's operation, repair and maintenance funds, the project was deprived of the essential funds to implement an adequate program of ongoing maintenance and regular repair, as well as necessary capital improvements. The result was the growth in squalor, disrepair, and dangerous and unhealthy conditions that inevitably ensued. By 1997, when petitioners initiated this legal action, the number of violations of local building codes had reached a staggering fifteen hundred ninety-five (1,595), with

eleven hundred eighty-eight (1,188) of these deemed hazardous to the lives, health and/or safety of the residents.[2]

That these conditions, and the concomitant injuries to the value of the petitioners' leaseholds, were in fact caused by the long-term looting of the very funds needed to operate, maintain, repair and improve the project must be taken as true for purposes of a motion to dismiss. What is at issue in this case, and what is discussed below, is: (a) whether the fact that because the predicate acts of mail fraud committed by defendants were directed to HUD, as overseer and enforcer of the HAP contract on the petitioners' behalf, rather than to petitioners to whom performance of the HAP contract's obligations and delivery of its benefits was owed, automatically precludes petitioners from establishing defendants' conduct as the proximate cause of their injuries, and necessarily renders their injuries derivative of those suffered by HUD; (b) whether the courts below extended the proximate cause analysis of *Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258 (1992) beyond the language and logic of its holding; and (c) whether it was erroneous for the Court below to treat the mail and wire fraud statutes as containing the elements of common law fraud, including misrepresentation and reliance, by holding ". . . that the tenants could not establish that their injuries were proximately caused by the alleged RICO violations; [because]

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[2] The District Court opinion speculates that the poor conditions at the Medgar Evers Houses might have resulted from " . . . the defendants' poor management of the housing project." *Medgar Evers Houses Tenants Ass'n., et. al v. Medgar Evers Houses Associates, L.P.*, 25 F. Supp.2d 116, 121 (E.D.N.Y. 1998). This not only ignores the allegations of the complaint, which should be taken as true for purposes of the motion to dismiss, but also disregards the fact that the defendant management companies had met the rigorous HUD regulations requiring that they demonstrate their competency, capacity and experience in such management. (24 C.F.R. §§ 265.10 (a)(2) and (4) and 200.219).

the defendants made misrepresentations only to HUD, not to the tenants directly." (emphasis added). (Decision below at 5a).

The conflicts among the circuits on the various proximate causation issues described above have produced widely varying interpretations of the meaning of "direct" causation in civil RICO actions based upon mail and wire fraud, the appropriate scope of proximate causation inquiry, and the competing "convergence vs. non-convergence" theories regarding the elements of mail and wire fraud when those offenses serve as predicate acts in civil RICO actions.

REASONS FOR GRANTING THE WRIT

I. THERE IS A FUNDAMENTAL CONFLICT BETWEEN CIRCUIT COURTS OF APPEAL REGARDING PROXIMATE CAUSE IN CIVIL RICO CASES PREDICATED UPON MAIL AND/OR WIRE FRAUD, WHEREIN THE SECOND AND FOURTH CIRCUITS HAVE EXPRESSLY ADOPTED "CONVERGENCE THEORY" WHILE THE THIRD AND FIFTH CIRCUITS HAVE EXPRESSLY REJECTED IT.

In civil RICO cases involving predicate acts of mail and wire fraud, the most controversial and hotly disputed conflict among the Circuit Courts of Appeal and among various federal district courts, is the issue of "convergence theory." The advocates of convergence theory argue that, in order to establish both standing and proximate causation, a plaintiff must in every case be both deceived by the predicate acts and injured by them. The opponents of this convergence-of-identity requirement assert that many potential plaintiffs have been directly and proximately injured by misrepresentations made to and relied upon by third parties.

Both the Third and Fifth Circuits reject convergence theory. The Fifth Circuit Court of Appeals has repeatedly held that, in the context of a civil RICO action based upon a pattern of mail and/or wire fraud acts in furtherance of an overall scheme to defraud, that "Our guideline for the elements of RICO mail fraud is: 1) a scheme to defraud by means of false or fraudulent representation, 2) interstate or intrastate use of the mails to execute the scheme, 3) the use of the mails by the defendant connected with the scheme, and 4) actual injury to the plaintiff. *In re Burzynski*, 989 F.2d 733 at 741 (5th Cir., 1993); *see also Abell v. Potomac Insurance Co. of Illinois*, 946 F.2d

1160 at 1167 (5th Cir. 1991). Thus, in the Fifth Circuit, the civil RICO plaintiff is not required to prove reliance on fraudulent mailings to prove proximate cause. *Armco Indus. Credit Corp. v. SLT Warehouse Co.*, 782 F.2d 475, 481-82 (5th Cir. 1986) (justifiable reliance not required to plead civil RICO predicated on mail fraud; "[b]y confusing mail fraud with common law fraud, [defendant's] argument falls wide of the mark."). Furthermore, the Fifth Circuit Court of Appeals has properly followed the admonition of this Court in *Holmes, supra*, to recognize the virtual impossibility of establishing a black letter rule of proximate cause that will dictate the result in every case, and instead, determines proximate cause through an inquiry informed by the broad range of considerations embodied in that concept. *Khurana v. Innovative Health Care Systems*, 130 F.3d 143, 147 and n.5 (5th Cir. 1997), *vacated as moot*, 119 S.Ct. 442 (1998).

The Third Circuit Court of Appeals, in *Tabas v. Tabas*, 47 F.3d 1280, at 1294, n.18, (3d Cir. 1995) has held that, "Defendants' assertion that the mailings involved must themselves be relied upon by the victim of the fraud in order for a RICO claim to be established is inaccurate. As this Court stated in *Kehr Packages*, 'completely innocent' mailings can satisfy the mailing element."[3]

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[3] The *Tabas* court also held that in civil RICO complaints based on predicate acts of mail fraud, the Court is required ". . . to look beyond the mailings and examine the underlying scheme or artifice. Although the mailing is the actual criminal act, the instances of deceit constituting the underlying fraudulent scheme are more relevant to the continuity analysis." *Tabas*, 47 F.3d. at 1294, citing *Kehr Packages v. Fidelcor, Inc.*, 926 F.2d 1406, 1414 (3d Cir. 1991). Petitioners contend that examination of the fraudulent scheme is at least as relevant to sound proximate cause inquiry as it is to continuity analysis. In *Rodriguez v. McKinney*, 878 F. Supp. 744, 749 (E.D.Pa. 1995), the Court supported petitioners' view, holding: "In *Tabas v. Tabas*, . . . its most recent RICO pronouncement, the Third Circuit clarified in a footnote that

These holdings are squarely in conflict with the holdings of the Court below in this case and with decisions by the Fourth Circuit which, for purposes of establishing proximate cause, required the predicate acts of mail and/or wire fraud to contain fraudulent misrepresentations that were directly sent to and relied upon by petitioners. Thus, while the approach of the Fifth and Third Circuit Courts of Appeal would not add the additional elements of misrepresentation and reliance to the mail and wire fraud predicate acts for purposes of civil RICO, and, instead, would adopt the broad, common law proximate cause inquiry endorsed by this Court in *Holmes*, both the Court below and the Fourth Circuit Court of Appeals have adopted the restrictive, "black letter rule" approach to determining proximate cause which *Holmes* disapproves.

The Court below held that because the misrepresentations here were made to HUD, the petitioners' injuries "are therefore necessarily derivative of injuries sustained by HUD," and concluded that petition-petitioners "[could] allege no direct injury." The Court below therefore held that because petitioners did not receive the fraudulent mailings, they were precluded as a matter of law from bringing this claim.

Similarly, in *Brandenburg v. Seidel*, 859 F.2d 1179, 1187-88, n.10 (4th Cir. 1988) *rev'd on other grounds, Quackenbush v. Allstate Ins. Co.*, 517 U.S. 706 (1996), the Fourth Circuit held that the predicate acts of mail fraud themselves must be not only the direct and proximate cause of the injuries, but also that ". . . while . . . it is not necessary to establish detrimental reliance by the victim in order to make out a violation of the federal mail fraud statute . . . *such reliance is necessary to establish injury to business or property 'by reason*

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victims of a RICO mail fraud need not demonstrate reliance on the predicate mailings themselves in order to allege a viable claim."

of a predicate act of mail fraud within the meaning of §1964(c)."[4] (emphasis added).

Thus, the requirement in the Second and Fourth Circuit Courts of Appeal that, for civil RICO purposes alone, the mailings that constitute the predicate acts must contain misrepresentations which are directly relied upon by the victim imposes severe limitations upon those who may recover under §1964(c) that are not imposed in the Third or Fifth Circuit Courts of Appeal.

The First Circuit Court of Appeals has also spoken on the question of convergence theory, although in the context of criminal prosecutions under the mail and wire fraud statutes. In *United States v. Christopher*, 142 F.3d 46 (1st Cir. 1998), the Court considered, apparently for the first time, whether the mail and wire fraud statutes were violated when the party deceived by the fraudulent communication was *not* the party who was deprived of money or property. In emphatically rejecting convergence theory, the Court held:

> Turning to whether we should now adopt a convergence theory, we see little reason to do so. Nothing in the mail and wire fraud statutes requires that the party deprived of money or property be the same party who is actually deceived. The phrase 'scheme or artifice . . . for obtaining money or property by means of false or fraudulent pretenses, representations or promises,' 18 U.S.C. § 1341, is broad enough to

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[4] Even the Fourth Circuit appears to have questioned, but not expressly disturbed, the rigid and restrictive holding of *Brandenburg*. *See Mid-Atlantic Telecom, Inc. v. Long Distance Services*, 18 F.3d 260, 263 (4th Cir. 1994).

> include a wide variety of deceptions intended to deprive another of money or property. *See United States v. Evans*, 844 F.2d 36, 39 (2nd Cir. 1988). We see no reason to read into the statutes an invariable requirement that the person deceived be the same person deprived of the money or property by fraud. *If, for example, the role of a government regulator is to protect the monetary interests of others, a scheme to mislead the regulator in order to get at the protected funds will affect 'property rights' as required in McNally.* [5]

142 F.3d at 53 (emphasis added).

The context of *United States v. Christopher*, *supra*, is different from the case at bar only to the extent that the identical mail and wire fraud statutes are being employed for different purposes. But there is no rational basis to assume that the Court's analysis in *United States v. Christopher*, *supra*, would not apply with equal force and logic when the same substantive statutes were being invoked as predicate acts in a RICO case, whether criminal or civil. The criminal defendant Christopher was accused of intentionally deceiving state insurance regulators assigned to protect the property and financial health of insurance companies in order to siphon off millions of dollars from those companies.

The respondents in this case, in order to loot the project account, allegedly subverted both federal regulations and contract obligations by deceiving HUD officials assigned to protect the living conditions of the residents, as to the physical

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[5] Referring to *McNally v. United States*, 483 U.S. 350 (1987).

state, operational and repair plans, and fiscal integrity of the project. In both *Christopher* and the instant case, the wrongdoers were obliged to deceive government regulators in order to "get at the protected funds," injuring the property rights of those entitled to the use or benefit of those funds. *Christopher*, 142 F.3d at 54.

Thus, insofar as it can be fairly assumed that the First Circuit would apply its analysis of convergence theory in *Christopher* to a situation in which the identical statutes were invoked at predicate acts in a civil RICO context, the Second and Fourth Circuits are also effectively in conflict with the First Circuit Court of Appeals as well.

Exacerbating the conflict between the circuits set forth above is the chaotic state of the law governing these questions among the district courts within the Second Circuit Court of Appeals. Within the Second Circuit, no fewer than nine district court cases share the Third Circuit's rejection of convergence theory. *See Ifill v. West*, No. 96CV6308 (SJ), 1999 WL 690144 (E.D.N.Y. Aug. 24, 1999); *Sterling Interiors Group, Inc. v. Haworth, Inc.*, No. 94 CIV. 9216 (CSH), 1996 WL 426379 (S.D.N.Y. Jul. 30, 1996); *Phoenix Home Life Mutual Ins. Co. v. Brown*, 857 F. Supp. 7 (W.D.N.Y. 1994); *Volman Distributors, Inc. v. New York Post, Inc.*, 825 F. Supp. 1153 (S.D.N.Y. 1993); *Trautz v. Weisman*, 819 F. Supp. 282 (S.D.N.Y. 1993); *Scharf v. Claridge Gardens*, No. 88 CIV. 2047 (JAC), 1990 WL 186879 (S.D.N.Y. Nov. 21, 1990); *Metromedia Co. v. Fugazy*, 753 F. Supp. 93 (S.D.N.Y. 1990), *aff'd. as amended*, 983 F.2d 350 (2d Cir. 1992); *Shaw v. Rolex Watch, U.S.A., Inc.*, 726 F. Supp. 969, 972-3 (S.D.N.Y. 1989); and *Galerie Furstenburg v. Coffaro*, 697 F. Supp. 1282 (S.D.N.Y. 1988). By contrast, at least four district court cases have embraced convergence theory. *See, e.g., Burke v. Dowling*, 944 F. Supp. 1036 (E.D.N.Y. 1995); *B.V. Optishce*

Industrie De Oude Delfl v. Hologic, Inc., 909 F. Supp. 162, 170 (S.D.N.Y. 1995), *recons. denied*, 925 F. Supp. 162 (S.D.N.Y. 1996); *Gruntal & Co. v. San Diego Bancorp*, 901 F. Supp 607 (S.D.N.Y. 1995); and *Red Ball Interior Demolition Corp. v. Palmadessa*, 874 F. Supp. 576 (S.D.N.Y. 1995).[6]

Moreover, in at least one other Circuit which has not definitively decided this issue, similar confusion reigns. Compare *Stamp v. Brown*, Nos. 81 C 1475, 80 C 6251, 1991 WL 628, *2 (N.D.Ill. Jan. 2, 1991), with *United States v. Keane*, 678 F. Supp. 708, 711 (N.D.Ill. 1987), aff'd 852 F.2d 199 (7th Cir. 1988).

As is plain from the district court decisions cited above, the courts within at least the Second and Seventh Circuits have become a legal lottery on the issue of proximate causation and "convergence" theory in civil RICO cases based upon mail and wire fraud.[7] Moreover, because the decision below was rendered in the form of a summary order, and is not binding on the district courts, confusion will continue to reign both among the circuits and within the Second Circuit until this Court speaks definitively on the questions presented here.

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[6] The district court decisions cited here are merely a sampling of the competing positions held by these courts in the Second Circuit, and should not be construed as a comprehensive list of cases which have spoken on these issues.

[7] At present, the district courts simply choose from among the various approaches the one that most appeals to them. Thus in the most recently decided district court case cited above, the Court held: "This Court concurs in Judge Haight's analysis and follow Sterling Interiors, Trautz and Shaw in concluding that a plaintiff may satisfy RICO's standing requirement by pleading that they were injured as proximate result of fraudulent acts directed at third parties." *Ifill*, 1999 WL 690144 at *11.

II. THE QUESTIONS PRESENTED BY THE DECISION BELOW REFLECT A SUBSTANTIAL DEPARTURE FROM THE PROXIMATE CAUSE ENQUIRY REQUIRED BY *HOLMES*, THE EFFECT OF WHICH WOULD PRECLUDE ENTIRE CATEGORIES OF PERSONS SUFFERING RICO INJURIES FROM THE REMEDIES PROVIDED BY THE STATUTE.

The importance of the holding by the Second Circuit Court of Appeals is that it misconstrues this Court's holding in *Holmes*:

a. to categorically exclude from use of the civil RICO statute entire classes of private plaintiffs, such as third party beneficiaries of a fraudulently breached contract, who are clearly within the zone of interest of those whom Congress intended to protect, although the injuries they suffered resulted directly from misrepresentations made to others;[8]

b. to prohibit those victims of a RICO enterprise most directly damaged in their business or property by the defendants' criminal conduct from seeking the dissolution of the enterprise that injured them and an injunction against its principals from engaging in the same or similar activities, relief uniquely provided by the civil RICO statute, as well as compensation for those injuries;

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[8] Other classes of potential plaintiffs who may be directly injured by defendants' fraudulent misrepresentations to third parties acting as plaintiffs' representatives include: persons dependent upon government regulators for the protection of their property; persons acting through their business agents or fiduciaries, owners of property entrusted to bailees, beneficiaries of trusts or estates who rely on executors or administrators, and disabled people who must act through the holder of their power of attorney.

c. to limit proximate cause inquiry in a civil RICO context to the immediate effects of the predicate acts isolated from and without reference to the fraudulent scheme they effectuated;

d. to effectively modify the federal mail and wire fraud statutes by judicially importing the requirements of (i) a misrepresentation made directly to the plaintiff/victim, and (ii) direct and immediate reliance upon those statements by the plaintiff/victim; and

e. to adopt the controversial "convergence theory" requiring that, in civil RICO actions based on predicate acts of mail and/or wire fraud, the person directly deceived and the person injured must be identical in order to satisfy the proximate cause requirement.

These judicially created obstacles to the satisfaction of the civil RICO proximate cause test have extended the proximate cause standard of *Holmes* far beyond any reasonable interpretation of that decision, and have worked a manifest injustice upon the one hundred eighty-one petitioners in this case who have suffered a drastic, long-term loss in the value of their leaseholds, and may now face a return of this housing project to the operational custody and control of the defendants.[9] (The erroneous nature of the interpretation given *Holmes* by the Courts below is argued at POINT III, *infra*.)

As this Court has yet to address the questions presented here, a distinct threat exists that other circuits will answer them

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[9] Although the "continuity" element of civil RICO actions is not at issue here, the fact that the tenants' action was dismissed not only leaves defendant MEHALP as owner of the project, but presents a real risk that it will resume its operational control.

in the unduly restrictive and unjust manner that is reflected in the decision below. (*See Holmes*, 503 U.S. at 286, 289-90, concurring opinions of Justices O'Connor and Scalia, regarding the danger of statutorily unwarranted restrictions upon and inconsistent standards for pleading proximate causation.)

The facts of this case, and the decisions below, offer this Court the opportunity to clarify the meaning of *Holmes* and resolve many of the most vexing and controversial questions regarding civil RICO proximate cause that remain unanswered.

III. THE PETITIONERS, AS THIRD PARTY BENEFICIARIES OF DEFENDANTS' CONTRACT WITH HUD, WERE NOT PRECLUDED FROM ESTABLISHING DIRECT INJURY MERELY BECAUSE DEFENDANTS' MISREPRESENTATIONS WERE MADE ONLY TO HUD.

A. The Court Below Misconstrued the Proximate Cause Holding of *Holmes*.

The holding of the Court below expresses an absolute requirement that only the recipient of a mailing containing a material misrepresentation upon which the recipient detrimentally relies can satisfy the proximate cause requirement of direct injury that must be pleaded under civil RICO. In doing so, the Court below relies upon this Court's decision in *Holmes*, despite the fact that all that *Holmes* requires is a showing of a direct relationship between the injury suffered and the misconduct alleged by the plaintiffs.

This exceptionally restrictive interpretation of the *Holmes* holding excludes from the protection and remedies of

civil RICO entire categories of persons directly and intentionally injured by the fraudulent conduct of the participants of the RICO enterprise (*see* n.3, *infra*). The excluded group in this case is comprised of third party beneficiaries of contracts in which the RICO defendants are promisors. Under such third party beneficiary contracts, the promisee typically reserves for itself the right and duty to oversee and enforce the promisor's performance of the agreement; to wit, the delivery of the benefits of the contract to the third party beneficiary. *Owens v. Haas*, 601 F.2d 1242, 1250 (2d Cir. 1979). But the contract's paramount purpose is to ensure that the third party receives the benefit. *Id.*

Accordingly, when the promisor breaches the contract -- in this case by the long-term looting scheme -- it is typically the individual beneficiaries, rather than the promisee, who are deprived of the benefits of the contract and are, therefore, the most directly and grievously injured.

In the case at bar, the decision below has resulted in the illogical and unjust result of categorically excluding the petitioners, who are in direct privity of contract with the defendants, from alleging direct injury by reason of the fraudulent breach of that contract, despite the clear factual reality that it was the tenants who were the primary victims of defendants' fraudulent scheme and who were the only parties who suffered damage to their property recognized under §1964(c).[10] The apparent reasoning of the Court below is stated

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[10] HUD did not "own" the money it paid to defendants on the petitioners' behalf to deliver safe, decent and sanitary housing to the petitioners. Rather, this money was appropriated by Congress for use at this specific housing project to deliver a specific level of housing quality to these specific residents. Were HUD to sue for restitution of the stolen funds, it would be legally obliged to return those funds to the project account, rather than to a

only as a factually and legally incorrect conclusion that the petitioners' injuries were "necessarily derivative of injuries sustained by HUD". (Decision below, p.6a).

The conclusion by the Court below that petitioners' injuries were necessarily derivative of injuries to HUD was factually incorrect for the following reason: the "injury to property" suffered by HUD was the money it ultimately had to pay to make the repairs and improvements and provide the services that were supposed to have been paid for by the misappropriated funds. By contrast, the primary damage to the petitioners' property was the drastic reduction in the value of their leaseholds. Specifically, the petitioners were contractually entitled to living conditions that met federal Housing Quality Standards (i.e., conditions that were "safe, decent and sanitary"). The monetary value put on such living conditions is set forth in the Housing Assistance Payment agreement as the "contract rent" for each unit. The more conditions fell below such federal standards, the lower the monetary value of each tenant's occupancy.[11] Thus, while both HUD and the petitioners would have had standing to sue the defendants for breach of the HAP contract, *see In Re Spong*, 661 F.2d 6, 10 (2d Cir. 1981), and obtain restitution to the project account of the stolen monies, only the tenants would have standing to seek compensation for the drastic reduction in the value of their leaseholds that resulted from defendants' looting scheme.

HUD general account.

[11] In New York, there is a routine and commonly utilized formula for establishing "rent abatement" damages, in which the trier of fact determines the percentage by which the value of an apartment unit was reduced due to poor conditions, and awards this percentage as a fraction of the monthly rent times multiplied by the number of months the poor conditions persisted.

Moreover, the conclusion that petitioners' injuries were "necessarily derivative" was legally erroneous because the Court below ignored the classic considerations informing proximate cause inquiry, and focused only on the fact that defendants' mailings were transmitted to HUD rather than plaintiffs. In adopting such a mechanical approach, the Court below refused even to consider that defendants communicated with HUD rather than the tenants simply as a matter of tactical necessity. Specifically, defendants were required by the HAP contract and accompanying federal regulations to submit to HUD certifications regarding living conditions, as well as monthly and annual financial statements and other sworn and unsworn representations regarding the operation, maintenance and fiscal integrity of the project. These submissions enabled HUD to enforce performance of the HAP contract on the tenants' behalf.

The tenants relied upon HUD, which acted as their fiduciary agent for purposes of enforcing the terms of the contract, to ensure that they received the benefits of the contract. When HUD, by reason of the predicate acts of mail and wire fraud, failed to discharge its enforcement responsibilities, the foreseeable and, indeed, inevitable consequences ensued: the steady deterioration of living conditions at Medgar Evers Houses.

As the defendants were accountable for their performance of the contract to HUD, rather than petitioners, they simply had no need to lie directly to them. However, defendants' misrepresentations to HUD about the conditions at the project and concealment of their looting from HUD were nonetheless essential not only to obtain monthly subsidy payments, but to avoid official detection of their long term scheme to defraud the project's operation and maintenance account.

B. The Highly Restrictive Proximate Cause Inquiry Employed Below Precludes the Broad Common Law Inquiry Recommended In *Holmes* And Adopts A "Black Letter Rule" Which *Holmes* Repudiates.

It could not be clearer that defendants' decision to direct their lies to HUD rather than the petitioners was dictated by purely logistical considerations, and should play little if any part in any proximate cause inquiry. On the contrary, a common law inquiry would consider such factors as:

a. whether defendants' decade-long pattern of fraudulent misrepresentations and concealment transmitted by mail and/or wire to HUD, as the administrator and enforcer of the tenants rights under the contract, played a material and substantial role in enabling defendants to loot operation and maintenance funds while avoiding official detection;

b. whether the injuries which petitioners alleged to be the natural and foreseeable consequences of the fraudulent scheme the defendants implemented through the pattern of predicate acts were direct or derivative of the injuries suffered by HUD; [12]

c. whether the practical and policy concerns underlying proximate causation, including "ideas of justice," foreseeability, and avoidance of attenuated claims by remote

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[12] It is self-evident that if defendants loot the funds intended to provide uniformed security, an increase in crime will result: if they loot the funds for extermination services, rodent infestation will increase; if they misappropriate roof repair money, leaks will persist, and so on.

parties, are met by permitting those such as petitioners herein, who are in direct privity of contract with the defendants, and who have been fraudulently deprived of the benefits promised by defendants; and

d whether the injuries alleged were more likely than not caused by an independent event and/or party than by the misconduct alleged against the defendants.

In deciding the proximate cause issue in *Holmes*, this Court did not base its holding on the fact that the non-purchasing customers were not the parties deceived by the securities fraud. On the contrary, the Court suggested that there need not be a "convergence" of identity between the person deceived and the person injured in order to satisfy the direct injury element of the proximate cause test.[13] Rather, this Court noted that "our use of the term 'direct' should merely be understood as a reference to the proximate cause enquiry that is informed by the concerns set out in the text." *Id.* at 273, n.20.

Nevertheless, the Court below equated the existence of a direct injury with the convergence in identity of the party directly deceived and the party injured, and concluded, as a matter of law, that any injury resulting from a misrepresentation the defendant made to someone other than petitioners was necessarily indirect and derivative. Such a holding cuts off any further causation inquiry before it begins, and excludes from

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[13] In footnote 19 of *Holmes*, 503 U.S. at 272, the Court observed with respect to a "parking" scheme alleged against the defendants who, without making any false statements to their customers, parked stock in their accounts and then "bought" or "sold" the stock in a series of sham transactions, that "We do not rule out that, if, by engaging in the parking transactions, the conspirators committed mail fraud, wire fraud or 'fraud in the sale of securities' . . . the broker-dealers' customers might be proximately injured by these offenses."

consideration the entire array of common law proximate cause factors recognized by this Court as central to determining whether a civil RICO injury was sufficiently direct and attributable to the defendants' misconduct to meet the proximate cause test. This ultra-restrictive inquiry is a particularly egregious departure from the broader common law inquiry recommended in *Holmes* because, unlike the facts of *Holmes*, no intervening event or alternative explanation for plaintiffs' damages has even been suggested.[14]

For all of the above reasons, the restrictive interpretation of the *Holmes* proximate cause test in civil RICO actions adopted and applied in this case by the Second Circuit Court of Appeals distorts the holdings of this Court and should be reversed.

IV. THE HOLDING OF THE COURT BELOW, IN EFFECT, JUDICIALLY MODIFIES BOTH THE CIVIL RICO STATUTE AND THE MAIL AND WIRE FRAUD STATUTES, AND DISREGARDS THE INTENT OF CONGRESS TO INCLUDE WITHIN THE PURVIEW OF CIVIL RICO THE TYPE OF "EGREGIOUS CRIMINAL CONDUCT"

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[14] In *Holmes* there were at least two intervening events which caused plaintiffs' injury: the revelation of the securities fraud to the market, causing the price to plummet, and the subsequent insolvency of the broker-dealers. In this case, the deterioration of living conditions was the foreseeable result of defendants' theft of operation and maintenance funds. A specific example alleged in plaintiffs' complaint is the claim the defendants misappropriated hundreds of thousands of dollars per year specifically earmarked to provide on-site uniformed security guards. The theft of that money was followed by a steady increase in on-site crime. No intervening event or circumstance, akin to the public revelation of the securities fraud or the insolvency of the *Holmes* case was even suggested below.

THAT DEFENDANTS COMMITTED IN THIS CASE.

There is no dispute that, while there is an implicit "materiality" requirement in the mail and wire fraud statutes, *United States v. Gaudin*, 515 U.S. 506 (1995), there is no requirement that the mail or wire transmissions themselves contain a misrepresentation or that someone acts in reliance upon them. Rather, these statutes require only that there be a scheme or artifice to defraud, for the purpose of obtaining money or property, and the use of the mail and/or wires in furtherance of that scheme. *See, e.g., Neder v. United States*, 527 U.S. 1, 119 S. Ct. 1827, 1841 (1999). In *Neder, supra*, this Court held that "[t]he common law requirements of 'justifiable reliance' and 'damages', for example, plainly have no place in the federal fraud statutes. *See, e.g., United States v. Stewart*, 872 F.2d 957, 960 (10th Cir. 1989) ('[Under the mail fraud statute], the government does not have to prove actual reliance upon the defendant's misrepresentations'); *United States v. Rowe*, 56 F.2d 747, 749 (2nd Cir. 1932) (L. Hand). ('Civilly of course the [mail fraud statute] would fail without proof of damage, but that has no application to criminal liability'")."

It is noteworthy that even the difference expressed in *Neder, supra*, between the criminal and civil showing based on mail fraud is the presence of a "damage" rather than a "reliance" component in the civil case. However, neither a criminal nor a civil case based on mail fraud contains the element of justifiable reliance.

Yet the Court below has treated the predicate acts alleged in the complaint as if, for civil RICO purposes alone, the victims of the scheme to defraud necessarily had to be the recipients of transmissions containing fraudulent statements upon which they justifiably relied. This is unsupported by either

the statutory language of any portion of 18 U.S.C. §§1961 - 1964, 18 U.S.C. §1341 or 18 U.S.C. §1343, or judicial precedent established by this Court or any Circuit Court. Moreover, it disregards fundamental principles of statutory construction. As this Court held in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), ". . . if Congress had legislated the elements of a private cause of action for damages, the duty of the Judicial Branch would be to administer the law which Congress enacted; the Judiciary may not circumscribe a right which Congress has conferred because of any disagreement it might have with Congress about the wisdom of creating so expansive a liability."

It is clear that, whatever the motive of the Court below, it has substantially circumscribed a private cause of action which Congress has conferred by radically modifying the elements that Congress has legislated.

A. The Legislative History of § 1964(c) Clearly Demonstrates the Intent of Congress that the Predicate Acts of Mail and Wire Fraud Be Considered Together With the Criminal Scheme They Serve in Order to Determine Whether Defendants Have Engaged In the Sort Of "Egregious Criminal Conduct" that Warrants Employment of the Civil RICO Remedy.

The facts of this case contain all of the factors which Congress intended to be present in order to limit the use of civil RICO's remedies by private litigants. The legislative history of civil RICO states, inter alia, that ". . . civil RICO will continue to be available to plaintiffs for use against the most serious kinds

of fraud, such as that in many of the savings and loan and bank fraud cases. It leaves in place a procedure *for attacking other major frauds and other significant criminal conduct,* but it will preclude its use in routine commercial and other disputes where much of the past abuse has occurred." (emphasis added). H.R. Rep. No. 102-312, (1991).

It is a matter of common knowledge, often announced in the media in the form of new initiatives by HUD to eliminate fraud in the national Section 8 programs, that what HUD calls "equity skimming schemes" are endemic throughout its low-income rent subsidy program. Indeed, HUD and the media have frequently attributed the looting of project funds by unscrupulous owners and managers as the principal cause of deterioration in and abandonment of many of its projects. Yet, because of budgetary constraints and drastic personnel reductions, HUD is increasingly less able to discharge its duties to the residents of these projects to enforce both federal housing regulations and the terms of its HAP contracts with specific owners. As third party beneficiaries of HAP contracts who are being deprived of the benefits of those contracts by looting schemes such as that alleged in this case, tenants actually make ideal civil RICO plaintiffs for purposes of serving the interests identified by Congress. Thus, as H.R. No. 102-312 observes, ". . . these civil suits would *supplement government action* and would attack real criminal conduct -- not just contract disputes written up to sound like crimes. These cases should, therefore, be the kind which might be brought by the Justice Department as criminal cases."[15] (emphasis added).

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[15] Indeed, an identical case to this one, *Drew Plaza Tenants Asso. v. Linden Realty, et al.*, 95 CIV. 52338 (RR), was brought by the tenants of another Section 8 project. That action, ultimately settled with defendants, alerted HUD and the United States Attorney's Office of the Eastern District of New York to the defendants' looting scheme and was directly responsible for

The petitioners are ideal as civil RICO plaintiffs for four reasons. First, because the tenants stand in direct privity with the defendants as both lessees of Section 8 leases and as third party beneficiaries of the HAP contract, they have the necessary legal standing to sue for both restitution of the looted monies and for damages for the diminished value of their leaseholds. By contrast, while HUD shares standing to sue defendants for the former, it cannot recover damages on the petitioners' behalf for the loss in value of their leaseholds.

Second, petitioners' lawsuit also serves the Congressional purpose of "supplementing government action" by directly including HUD as a non-culpable party. As mortgagee of these Section 8 projects and promisee of the HAP contracts, HUD is a necessary party to the litigation and is, therefore, entitled to all of the discovery obtained by plaintiffs, which discovery forms the evidentiary basis of any further criminal or punitive action the agency wishes to take against culpable owners and managers. This is a particularly efficient means of alerting the responsible government agency of wrongdoing and sharing the evidence gathered by plaintiffs with that agency in a prompt manner.

Third, the tenants themselves, as occupants of the looted project, provide a vast source of information and evidence about the physical conditions of the project, and can be indispensable witnesses in any later prosecution, particularly in rebutting claims by defendants that they spent project monies to provide specific repairs and services.

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the indictments of the principals (*United States v. Mochkin et al.*, 98-CR-1161 (CA)) for defrauding the project of more than $2,000,000. (*The New York Times*, 12/25/98, Sec. B., page 1).

Fourth, civil RICO is the only remedy available to petitioners that provides for the dissolution of the enterprise and prohibition of its principals from engaging in the same or similar activities in the future.

That wholesale looting of monies intended to provide safe, decent and sanitary housing for the poor constitutes the "egregious criminal conduct" contemplated by House Report No. 102-312 seems self-evident. The owners and managers of Medgar Evers Houses, by operating their enterprise through a pattern of mail and wire fraud for more than a decade, dramatically decreased the value of petitioners' leaseholds. Permitting petitioners to bring this civil RICO lawsuit would clearly serve the public interest demanded by Congress (H.R. No. 102-312) by concretely aiding official investigation and prosecution of these wholesale frauds and deterring such conduct by others, and making the petitioners whole for the severe damage to their property.

CONCLUSION

The petition for a writ of certiorari should be granted.

Dated: February 14, 2000

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

THIS SUMMARY ORDER WILL NOT BE PUBLISHED IN THE FEDERAL REPORTER AND MAY NOT BE CITED AS PRECEDENTIAL AUTHORITY TO THIS OR ANY OTHER COURT, BUT MAY BE CALLED TO THE ATTENTION OF THIS OR ANY OTHER COURT IN A SUBSEQUENT STAGE OF THIS CASE, IN A RELATED CASE, OR IN ANY CASE FOR PURPOSES OF COLLATERAL ESTOPPEL OR RES JUDICATA.

At a Stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, Foley Square, in the City of New York, on the 16th day of November, one thousand nine hundred and ninety-nine.

PRESENT: HON. JOSEPH M. McLAUGHLIN,
HON. DENNIS JACOBS,
HON. ROBERT A. KATZMANN,
Circuit Judges.

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Amilia ABBOTT; Kanvra Abdul-Karim; Edwin Acervedo; Carolyn Adams; Deborah Alston; Patricia Alston; Marlene Anaya; Annie Barnes; Charise Barnes; Sheila Batts; Jeanine

Bell; Cecilia Benique; Clinton Biet; Teresita Bowman; Elizabeth Browde; Annette Brown; Cora Brown; Jerelyn Brown; Leona Brown; Robert W. Brown; Roberta Brown; Ramona Bryan; Cheryl Burke; Sandra Byrd; Debbie Cannon; Pernice Carroll; Hazel Carter; Marsha Carter; Louise Chaneyfield; Sonia Clintron; Karen Cleveland; Toni Cleveland; Cora Cofield; Belinda Collier; Gwendolyn Cooper; Shirley Cooper; Shirley Corley; Antonia Creel; Deborah Davis; Kim D. Day; Ruby Dicks; Monique Dorsey; Douglas Drayton; Lovellan Dunton; Mary Dyson; Robert Edward; Beatrice Estwick; Kahesa Farmer; Sally Farmer; Margaret Fason; Carmen Feliciano; Sheri-Ann Felix; Paulette Ferguson; Francine Fortune; Latisha Frederick; Dorthy Mae Gainyard; Estelle Gibson; Geraldine Giles; Margaret Gillyard; Ethel Gladden; Modesto Gonzalez; Pamela Gordon; Concencia Gorman; Ernestine Green; Elsie Griffin; Joan Griffith; Sheila Grimes; Remona Hall; Rachel Henderson; Crystal Hollins; Sylvia Holman; Lorena Holme; Gloria Howard; Flora Hudson; Virginia Jackson; Deborah Jones; Ethel Jones; Mattie Jones; Odessa Jones; Gregory Kearse; Gladys Kendrick; Loretta Knox; Ronald Knox; Wanda Knox; Albert Langston; Barbara Lewis; Odessa McKenzie; Jean Mabry; Joseph Maddox; Arlene Madison; Donna Mahon; Darene Mallery; Gloria Marcus; Luz Martinez; Diane Mashburn; Addie Mazyck; Brenda Michel; Joann Mitchell; Theresa Moody; Letona Moffett; Willena Moore; Medgar Evers Houses Tenants Association; Grace Morgan; Rachael Morris; Shalon Murdaugh; Rochelle Murdaugh; Edwina Murphy; Kisha nelson; John Nixon; Lee Anne Ogbewele; Cheryl L. Page; Barbara Paign; Vonzella Palmer; Vickie Parker; Gale Patterson; Jean Penn; Rosetta Pattiford; Minnie

Pierce; Essie Porter; Emma Pratt; Ronnie Pullian; Thelma Pullian; Bettie Ramizee; Carol Reddick; Raquel Rivera; Fdella Robinson; Idela Robinson; Charlotte Rodgers; Lola Rodgers; Linda Roy; Marsha Roy; Jessie Sanders; Lena Settles; Latoya Shannon; Mary Shipman; Theodore Simmons; Sylvia Simpkins; Carrie Simpson; Onella Simpson; Hazel Smalls; Sharron Smith; Sonia Smith; Latisha Spencer; Picola Spencer; Janice Staton; Jocynthia Stokes; Johnie Stovall; Carol Sutton; Evelyn Sutton; Alison Taylor; Maxine Taylor; Chester Thomas; Karen Thomas; Laraine M. Thomas; Monica Thomas; Shirley Thomas; Shana Thompson; Tenyatta Turpin Gregory; Aisha Tyler; Beverly Vaden; Virginia Vaughan; Gladys Vice; Clarice Wade; June Wallace; Sonia Wallace; Patricia Washington; Alissa Webb; Dorothy White; Banquetta Whitt; Michele Wike; Kathleen Wildmon; Dorothy Williams; Lavon Williams; Michelle T. Williams; Sarah Williamson; Nacomis Wilson; Cassandra Womack; Bonnie Worley; Evelyn Worrell; Darlene Wortham; Ethel Wright; Tywanna Wright Gardner,

Plaintiffs-Appellants,

v.

MEDGAR EVERS HOUSES ASSOCIATES, L.P.; Philip Rosenberg; Douglas Rosenberg; BPC Management Corporation; New York City Department of Housing Preservation and Development; Seymour Maslow; Richard Curtis; New England Management Company, Inc.,

Defendants-Appellees;

United States Department of Housing and Urban Development,

Defendant.

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No. 98-6275.

Appearance for Appellant:

NAOMI J. SCHRAG, New York, NY, (Lisa E. Cleary, Frederick B. Warder, Patterson Belknap Webb & Tyler, LLP, Richard J. Wagner, Jim E. Provost, Brooklyn Legal Services Corp. A., on the brief).

Appearance for Appellee:

FRANKLYN H. SNITOW, New York, NY, (Robert P. Devlin, Snitow & Cunningham, LLP, on the brief).

Appeal from a final judgment entered on October 23, 1998 in the United States District Court for the Eastern District of New York, (Gleeson, J.)

UPON DUE CONSIDERATION, IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the judgment is AFFIRMED.

Tenants in a federally subsidized low-income housing project brought this civil RICO suit against the owners and managers of the project alleging that the defendants engaged

in mail and wire fraud. It is alleged (i) that the defendants made false certifications regarding conditions at the project in monthly filings with the United States Department of Housing and Urban Development (HUD), and thereby induced the payment of federal subsidies; (ii) that the defendants submitted to HUD a series of false written statements assuring HUD that major repairs and improvements to the project were imminent; and (iii) that the defendants submitted to HUD monthly and annual financial statements that contained material misrepresentations about the project's operating costs. As a result of the alleged mail and wire fraud, the tenants claimed they "suffered the substantial diminution in both the value of their occupancies as well as in the value of the millions of entitlement dollars paid to the owner on behalf of [tenants] in the form of monthly rent subsidies."

The district court dismissed the complaint on the ground, inter alia, that the tenants could not establish that their injuries were proximately caused by the alleged RICO violation; the defendants made misrepresentations only to HUD, not to the tenants directly.

The district court's analysis, which is consistent with then-existing precedent, has been further supported by later decisions of this court. To state a claim under RICO, the tenants must allege that their "injuries were both factually and proximately caused by the alleged RICO violation." *In re American Express Co. Shareholder Litig.*, 39 F.3d 395, 399 (2d Cir.1994) (citing *Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258, 266 68 (1992)). "The causation

requirement, which is jurisdictionally mandated, has two different components. There must be 'transaction causation,' meaning that the misrepresentation must have led the plaintiffs to enter into the transactions at issue, and there must be 'loss causation,' meaning that the misrepresentation must be both an actual and a proximate source of the loss that the plaintiffs suffered." *Moore v. PaineWebber, Inc.*, 189 F.3d 165, 169 70 (2d Cir.1999) (*citing First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 769 (2d Cir.1994)).

The tenants here failed to establish loss causation because they failed to establish that the defendants' misrepresentations were a proximate source of the tenants' injuries. "[T]o plead a direct injury is a key element for establishing proximate causation, independent of and in addition to other traditional elements of proximate cause. Thus, the other traditional rules requiring that defendant's acts were a substantial cause of the injury, and that plaintiff's injury was reasonably foreseeable, are additional elements, not substitutes for alleging (and ultimately, showing) a direct injury." *Laborers Local 17 Health & Benefit Fund v. Philip Morris, Inc.*, 191 F.3d 229, 235 36 (2d Cir. 1999). As the district court concluded, the tenants can allege no direct injury because the defendants' misrepresentations were made only to HUD. The tenants' injuries are therefore necessarily derivative of injuries sustained by HUD. Because such derivative injuries are insufficient to establish proximate cause, see id. at 235-36, 238-39, the tenants cannot establish the loss causation necessary for RICO standing.

Accordingly, for the reasons set forth above, the final judgment entered on October 23, 1998 is hereby AFFIRMED.

United States District Court,
E.D. New York.

MEDGAR EVERS HOUSES TENANTS ASSOCIATION, et al.,

Plaintiffs,

v.

MEDGAR EVERS HOUSES ASSOCIATES, L.P., The United States Department of Housing and Urban Development, et al.,

Defendants.

No. 97-CV-2919 (JG).

Oct. 23, 1998.

Naomi Schrag, Patterson Belknap Webb & Tyler LLP, New York City, Richard J. Wagner, Brooklyn Legal Services Corp., "A", Brooklyn, NY, for Plaintiffs.

Franklyn H. Snitow, Snitow & Pauley, New York City, Medgar Evers Houses Assoc., L.P., BPC Management Corp., New England Management Corp., Philip Rosenberg, Douglas Rosenberg, Seymour Maslow, Richard Curtis, for defendants.

Zachary W. Carter, United States Attorney, Eastern District of New York, Brooklyn, NY, by Richard Molot, Assistant United States Attorney, for defendant United States, Department of Housing and Urban Development.

MEMORANDUM AND ORDER

GLEESON, District Judge.

The Medgar Evers Houses Tenants Association and 181 tenants bring this action against the Medgar Evers Houses Associates, Limited Partnership ("MEHALP"), BPC Management Corporation ("BPC"), the New England Management Company, Inc. ("New England Management"), and others, claiming violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961 *et seq.*, and New York State Real Property Actions and Proceedings Law (RPAPL) Article 7A, §§ 769-78. The defendants against whom relief is sought[1] have moved to dismiss the RICO claim on the ground that it fails to state a claim upon which relief could be granted. For the reasons set forth below, defendants' motion is granted.

FACTS

Medgar Evers Houses Tenants Association is an unincorporated association of tenants of the Medgar Evers Houses, a federally subsidized, low-income housing project

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[1] The United States Department of Housing and Urban Development ("HUD") and the Department of Housing and Preservation Development of the City of New York ("HPD"), named in the complaint as "co-defendants," are nominal defendants. HUD holds the mortgage on the property at issue and regulates the project, and HPD serves as the municipal agency charged with enforcement of New York City and State housing laws. Neither has taken a position on this motion. Unless otherwise noted, the term "defendants" refers only to MEHALP, BPC, New England Management, and the individual defendants.

consisting of nine buildings in the Bedford-Stuyvesant section of Brooklyn, New York. The individual plaintiffs are the tenants in 181 of the 315 apartment units located in the project. All of them participate in the federal program known as "Section 8" rental assistance.

Defendant MEHALP has owned the Medgar Evers Houses since 1985. Defendant BPC operated and managed the project for MEHALP from approximately 1985 to 1990. Defendant New England Management has operated and managed the project for MEHALP since 1990. The individual defendants are employees of BPC or New England Management.

A. The Statutory and Regulatory Framework

The Section 8 program helps low-income families obtain a wholesome place to live, see 42 U.S.C. § 1437f, furthering the National Housing Act's "goal of a decent home and a suitable living environment for every American family." 42 U.S.C. § 1441. To achieve this goal, HUD provides, among other benefits, mortgage insurance or direct mortgages to the private sector at below-market rates for development or purchase and maintenance of low-income housing for the duration of the mortgage. Section 8 rental assistance consists of monthly rent subsidy payments to the owners of qualifying housing projects, such as Medgar Evers Houses. The government subsidizes that portion of each tenant's total contract rent that exceeds 30% of the tenant's adjusted gross income.

HUD regulates Section 8 properties pursuant to various laws and regulations as well as through a Housing Assistance Payment ("HAP") Contract and a Regulatory Agreement between HUD and the property owner, in this case, MEHALP. Through the HAP Contract and Regulatory Agreement, HUD imposes on owners of Section 8 projects the duty to provide services and maintain the premises in compliance with HUD regulations and in conformity with state and local laws.

The government pays Section 8 rent subsidies on the tenants' behalf directly to the owner upon its (or its agent's) submission of a HUD form known as a "Housing Owner's Certification and Application for Housing Assistance Payments" ("Owner's Certification"). The Owner's Certification requires the owner to sign a statement that provides, in relevant part, that "all required inspections have been completed ... [and] the units for which assistance is billed are safe, decent and sanitary and occupied or available for occupancy." Complaint ¶ 47.

HUD retains the power and authority to replace non-performing management, to withhold subsidy payments and, if necessary, declare a default under the mortgage and regulatory agreement, and to become a "mortgagee in possession" or commence mortgage foreclosure proceedings.

B. The Conditions at the Medgar Evers Houses

HPD serves as the New York City agency responsible for inspecting residential apartment units for violations of various housing and building safety codes. HPD generally

conducts such inspections in response to tenant complaints or housing court disputes in which tenants allege conditions impairing building safety or habitability. Violations issued by HPD inspectors fall into three categories of severity. The most severe are designated "C" violations, issued for conditions that present immediate hazards to the health and/or safety of the tenants. These must be corrected within twenty-four hours. Next in severity are "B" violations, issued for hazardous conditions, which must be corrected within thirty days. The least severe are "A" violations, which cover non-hazardous conditions that must be corrected within six months. Plaintiffs allege that, as of the filing of their complaint in May 1997, a total of 1,595 housing code violations existed at Medgar Evers Houses, of which 1,188 were either "C" or "B" violations.

Between 1990 and the present, HUD has conducted at least six on-site inspections. These inspections found various types of repairs and maintenance needed in many areas, including elevators, exterior walls and foundations, water and sewage systems, insulation, electrical fixtures and systems, and heating systems. The inspectors also found a need for rodent and vermin extermination and a pervasive condition of mold and mildew throughout the project.

C. The Plaintiffs' Claims

Although HUD is named as a "co-defendant" in the complaint, plaintiffs have conceded that it is only a nominal defendant, from which no relief is sought unless the Court orders the dissolution of the RICO "enterprise" and places the project in receivership. See Complaint ¶ 3; Transcript of

Oral Argument, Jan. 9, 1998 ("Tr."), at 18-19. [2] Plaintiffs thus do not assert that federal jurisdiction arises because HUD is a party to this action. Rather, federal jurisdiction rests on their RICO claim and on supplemental jurisdiction under 28 U.S.C. § 1367. The complaint alleges that MEHALP, BPC, New England Management, and the individual defendants constituted an "associated in fact" "enterprise" within the meaning of 18 U.S.C. § 1961(4). Plaintiffs charge those defendants with violating 18 U.S.C. § 1962(c) and (d) by participating and conspiring to participate in the conduct of the affairs of the enterprise through a pattern of racketeering activity consisting of acts of mail fraud and wire fraud. Specifically, plaintiffs allege "three distinct types of mail and/or wire frauds." Complaint ¶ 45.

The first centers on the monthly Owner's Certification filed with HUD. As noted above, each such certification must contain a statement by the project owner that "all required inspections have been completed ... [and] the units for which assistance is billed are safe, decent and sanitary." Plaintiffs allege that in each Owner's Certification since December 1985, MEHALP made that statement knowing it to be false and misleading. The second type of fraud alleged in the complaint consists of statements made by MEHALP to HUD in response to its site inspection reports and management reviews conducted between 1986 and 1997. These letters,

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[2] "Similarly, the New York City Department of Housing and Preservation Development (HPD) is named as a nominal defendant because plaintiffs also assert a supplemental State claim for the appointment of an Article 7-A Administrator...." Complaint ¶ 3.

plans, and other written submissions (six are specified at Complaint ¶ 52) allegedly contained false and misleading statements to HUD regarding repairs and improvements to the project in order to "lull HUD into inaction." Complaint ¶ 54. The third type of fraud alleged by plaintiffs deals with monthly and annual financial reports which MEHALP submitted to HUD. These submissions allegedly contained false statements about MEHALP's costs and expenses in order "to conceal from HUD the 'diversion' and misappropriation of Project funds." Complaint ¶ 56.

Plaintiffs also allege conspiracy and substantive violations of 18 U.S.C. § 1962(b), contending that the defendants maintained their interest in, and control of, the charged enterprise through a pattern of racketeering activity. In addition to the RICO claims, plaintiffs allege violations of the New York Real Property Action and Proceedings Law based on the condition of the apartments in the project. Plaintiffs seek an order (1) dissolving the charged enterprise and placing its assets in receivership; (2) directing the defendants to divest themselves of their interest in the enterprise and in Medgar Evers Houses; and (3) enjoining the defendants from owning or managing public-assisted housing. They also seek treble damages under the RICO statute, an accounting, the appointment of an administrator under the RPAPL, [3] and attorneys' fees.

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[3] Defendants assert that the RPAPL claim is moot in light of a Stipulation and Order dated August 11, 1997, under which HUD became the Mortgagee-In-Possession of the Medgar Evers Houses and Jeffrey Goldstein was appointed a managing agent.

DISCUSSION

A. The Standard for Dismissal Under Rule 12(b)(6)

A federal court's task in determining the sufficiency of a complaint is "necessarily a limited one." *Scheuer v. Rhodes*, 416 U.S. 232, 236, 94 S.Ct. 1683, 40 L.Ed.2d 90 (1974). The inquiry focuses not on whether a plaintiff might ultimately prevail on her claim, but on whether she is entitled to offer evidence in support of the allegations in the complaint. *Id.* "Indeed it may appear on the face of the pleadings that a recovery is very remote and unlikely but that is not the test." *Id.* Rule 12(b)(6) warrants a dismissal only if "it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957); *see also Hamilton Chapter of Alpha Delta Phi, Inc. v. Hamilton College*, 128 F.3d 59 (2d Cir.1997). In addition, in ruling on defendant's motion, the Court must accept as true all the factual allegations in the complaint and must draw all reasonable inferences in favor of the plaintiff. *See Hamilton*, 128 F.3d at 59 (citing *Hospital Bldg. Co. v. Trustees of Rex Hosp.*, 425 U.S. 738, 740, 96 S.Ct. 1848, 48 L.Ed.2d 338 (1976)).

B. The RICO Claims

The RICO statute furnishes a private civil action to a person who has been "injured in his business or property by reason of a violation of" 18 U.S.C. § 1962. 18 U.S.C. § 1964(c). In order to prove a violation of § 1962, a plaintiff must prove that the defendant used money derived from a

pattern of racketeering activity to invest in an enterprise, acquired control of an enterprise through a pattern of racketeering activity, or conducted the affairs of an enterprise through a pattern of racketeering activity, or conspired to do any of those things. 18 U.S.C. § 1962(a)-(d). A pattern of racketeering activity requires, inter alia, at least two "acts of racketeering activity." 18 U.S.C. § 1961(5). The acts of racketeering activity alleged here consist of mail fraud and wire fraud in violation of 18 U.S.C. §§ 1341 and 1343, respectively.

1. The § 1962(c) Claim

The Supreme Court has interpreted the "by reason of" language in § 1964(c) as requiring not only actual causation, but proximate cause as well. *Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258, 268, 112 S.Ct. 1311, 117 L.Ed.2d 532 (1992). Holmes involved a RICO claim brought by the Securities Investor Protection Corporation ("SIPC"), a private nonprofit corporation established pursuant to a federal statute to provide financial protection to the customers of failed broker-dealers who were members of SIPC. SIPC had advanced nearly $13 million to the customers of two such broker-dealers and brought the RICO claim against Holmes and others on the theory that their fraudulent activity had prevented the broker-dealers from satisfying their obligations to those customers, thus triggering SIPC's statutory duty to reimburse those customers. 503 U.S. at 260-64, 112 S.Ct. 1311.

In rejecting SIPC's RICO claim, the Supreme Court focused on the distinction between injuries actually caused by

RICO violations and the narrower category of injuries "proximately" caused by them. The boundaries of the latter category have evolved as the result of a legal policy determination. As the Court put it, "Here we use 'proximate cause' to label generically the judicial tools used to limit a person's responsibility for the consequences of that person's own acts. At bottom, the notion of proximate cause reflects 'ideas of what justice demands, or of what is administratively possible and convenient.' " *Id.* at 268, 112 S.Ct. 1311 (quoting W. Page Keeton et al., *Prosser and Keeton on the Law of Torts* § 41, at 264 (5th ed.1984)). The Court concluded that in the civil RICO context, justice demands that a plaintiff demonstrate a direct relationship between the injury asserted and the RICO violation.

The Court identified several reasons for this directness requirement. First, "the less direct an injury is, the more difficult it becomes to ascertain the amount of a plaintiff's damages attributable to the violation, as distinct from other, independent, factors." *Id.* at 269, 112 S.Ct. 1311 (citation omitted). Second, extending the private RICO claim beyond the first level of injury would "force courts to adopt complicated rules apportioning damages among plaintiffs" at different levels of injury from the acts of racketeering, in order to prevent the risk of multiple recoveries. *Id.* Finally, the Court observed, there remains little need to address these complex issues, as the ability of directly-injured victims to bring suit generally serves the deterrent purpose of the private civil action. *See id.* at 269-70, 112 S.Ct. 1311.

Guided by these concerns, first expressed in the antitrust context, the Court concluded that SIPC was not a

proper RICO plaintiff. SIPC's claim would require a determination of whether the broker-dealers' customers' losses resulted from the alleged stock manipulation "as opposed to, say, the broker- dealers' poor business practices or their failures to anticipate developments in the financial markets." *Id.* at 273, 112 S.Ct. 1311. Putting that factual causation issue aside, the conferral of a cause of action on those indirectly injured would require the apportionment of the prospective recoveries among the various plaintiffs, "who would otherwise each be entitled to recover the full treble damages." *Id.* at 259, 112 S.Ct. 1311. Finally, "the law would be shouldering these difficulties despite the fact that those directly injured, the broker-dealers, could be counted on to bring suit for the law's vindication." *Id.* at 273, 112 S.Ct. 1311.

Those concerns equally apply to this case. The various false and misleading statements that constitute the acts of racketeering activity were all made to HUD. Plaintiffs do not allege that defendants made any of the representations underlying the mail and wire fraud allegations to the plaintiffs. Indeed, plaintiffs were not even aware of the false statements; in opposing defendants' statute of limitations argument, plaintiffs assert that they did not discover the scheme to defraud HUD until the spring of 1997. Plaintiffs' Mem. at 8.

The second-level injuries plaintiffs claim to have suffered are analogous to those alleged by the SIPC in Holmes and would impose similar burdens on the courts. If this RICO claim proceeds, the fact-finder would be required to determine whether the complained of conditions at the

Medgar Evers Houses in fact resulted from the false statements to HUD, as opposed to, for example, the defendants' poor management of the housing project. Putting that factual issue aside, permitting plaintiffs to maintain a treble damage action would seem to require an apportionment of possible recoveries among the directly defrauded party (HUD) and others indirectly injured by the fraudulent scheme, a group not necessarily limited to the plaintiff tenants.[4] Finally, as in *Holmes*, the law need not shoulder these difficulties. HUD itself can deter fraudulent statements to HUD. Owners who make the fraudulent statements face criminal prosecution under 18 U.S.C. § 1001, *see United States v. Mandanici*, 729 F.2d 914 (2d Cir.1984), and remain subject to civil penalties and other remedies under the HUD regulations.

Plaintiffs rely on the Second Circuit's articulation of the proximate cause requirement in *Hecht v. Commerce Clearing House, Inc.*, 897 F.2d 21, 23-24 (2d Cir.1990). In that case, the court stated that the RICO pattern or act must be a "substantial factor in the sequence of responsible causation,"

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[4] For example, a plumbing contractor with a contract to make the plumbing repairs at the project could allege that, as a result of false statements to HUD that plumbing repairs had been made, it was injured in its business, i.e., but for the fraud, it would have done the repair work. Such a contractor would also face an actual causation hurdle (in the absence of the fraud, would the defendants really have used the contractor to make the repairs?), but would be no further removed from the fraudulent conduct than the plaintiffs.

and the injury must be "reasonably foreseeable or anticipated as a natural consequence" of the defendant's fraudulent conduct. Plaintiffs here argue that the pattern of false representations to HUD enabled the defendants to get and keep federal funds that should have been expended for plaintiffs' benefit, and thus this pattern was a "substantial factor" in a sequence of events causing foreseeable injury to them. *See* Plaintiffs' Mem. at 18-19.

I disagree. Even accepting that the defendants' fraudulent statements to HUD constituted a "but for" cause of the conditions at the Medgar Evers Houses, those conditions were neither reasonably foreseeable when the defendants made the false statements nor the natural consequence of those statements. The racketeering acts allowed the defendants to receive continued, even increased, Section 8 funding. The defendants' failure to use the money to benefit the tenants did not flow from the misrepresentations made to HUD. This failure may have been a foreseeable result of plaintiffs' generalized allegations that defendants misappropriated federal funds, but plaintiffs do not include those allegations among the racketeering acts in the RICO claim. [5]

Second, plaintiff's reliance on *Hecht* ignores the fact that *Hecht* was decided before *Holmes*. Arguably, the proximate cause standard articulated by *Hecht*, and especially

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[5] I do not mean to suggest that the RICO claim would survive if it had included the misappropriations as racketeering acts.

its focus on the foreseeability of injury to the plaintiffs, requires some modification after Holmes, which focused on the directness of that injury. Indeed, it is not clear to me that the SIPC's claim in Holmes would have failed if the Court had applied to it the *Hecht* standard quoted above.

Although the Second Circuit has stated that "Holmes essentially endorsed [Hecht's] definition of proximate cause," *In re American Express Co. Shareholder Litig.*, 39 F.3d 395, 399 (2d Cir.1994), a careful reading of its decisions reveals a refinement of the *Hecht* formulation of the proximate cause requirement.

In *Hecht*, the court held that the plaintiff's injuries were not reasonably foreseeable or the natural consequence of the RICO violations because the plaintiff was "neither the target of the racketeering enterprise nor the competitor[ ] nor the customer[ ] of the racketeer[s]." 897 F.2d at 24 (internal quotations and citations omitted). More recently, the Second Circuit has made explicit a requirement, implied in Hecht and Holmes, that in order for a plaintiff to succeed on a RICO claim, the injuries alleged must be the "preconceived purpose" or the "specifically intended consequence" of the defendants' racketeering, or else they are not the "necessary result" or "foreseeable" consequence of those actions. *In re American Express*, 39 F.3d at 400; *see also Abrahams v. Young, & Rubicam, Inc.*, 79 F.3d 234, 237 (2d Cir.1996) (holding that plaintiff failed to establish RICO claim because he was not "the target of the racketeering enterprise[,] ... [t]hat is to say, [his] injuries did not flow from the harms that the predicate acts ... were intended to cause" (internal quotations

and citations omitted)), *cert. denied*, --- U.S. ----, 117 S.Ct. 66, 136 L.Ed.2d 27 (1996).

Thus, the cases in which RICO claims have failed involve racketeering acts directed at persons other than the plaintiffs. The claim in *Hecht* was brought by an employee who alleged fraudulent acts (such as forging customer signatures on orders and fabricating bills) committed by fellow employees and their agents against their customers. 897 F.2d at 22. In *Manson v. Stacescu*, 11 F.3d 1127 (2d Cir.1993), *cert. denied*, 513 U.S. 915, 115 S.Ct. 292, 130 L.Ed.2d 206 (1994), plaintiffs charged the defendants with numerous criminal acts committed as part of a scheme to loot a company. The plaintiffs, who were shareholders or employees of the company, or guarantors of its debt, lost their RICO claim because their injuries, unlike those of the corporate victim, were indirect. *See id.* at 1132; *see also In re American Express*, 39 F.3d at 399-401 (determining that shareholder derivative RICO claim failed because corporate officers' alleged conspiracy to defame rival company involved criminal acts directed at others, not at corporation); *Abrahams,* 79 F.3d at 238 (stating that intended targets of advertising firm's illegal scheme to obtain foreign account by bribery and other illegal acts were firm's competitors, and thus intended recipient of bribes, who was injured only by fallout from scheme's disclosure, could not maintain RICO claim).

On the other hand, RICO claims survive proximate cause-based motions to dismiss when the plaintiff stands as the target of the racketeering acts. In *GICC Capital Corp. v. Technology Fin. Group, Inc.*, 30 F.3d 289 (2d Cir.1994), *cert. denied*, 518 U.S. 1017, 116 S.Ct. 2547, 135 L.Ed.2d 1067

(1996), for instance, the plaintiff, a creditor of a corporation, brought a RICO claim against defendants who looted the corporation's assets, causing the corporation to default on his note. Although the circumstances in *GICC Capital* appear superficially similar to those in *Manson, supra*, the plaintiff in *GICC Capital* negotiated the note with the defendants while they looted the company and alleged fraudulent behavior directed at him in connection with the issuance of the note. *GICC Capital* at 292-93.

Measured against this standard, the RICO claims here fail. The alleged racketeering acts were "intended to mislead HUD," Complaint ¶ 52, "to lull HUD into inaction and induce it to forego punitive and/or remedial enforcement actions against MELHAP," Complaint ¶ 54, and "to conceal from HUD the 'diversion' and misappropriation of Project funds," Complaint ¶ 56. By plaintiffs' own formulation of their claim, HUD was the sole target of the alleged misrepresentations, and defendants induced HUD alone to part with millions of dollars. The plaintiffs were "not the intended targets of the RICO violations." *In re American Express*, 39 F.3d at 400; *see also In re Crazy Eddie Securities Litig.*, 714 F.Supp. 1285, 1291 (E.D.N.Y.1989) (dismissing RICO claim where racketeering acts were "directed not at Crazy Eddie but at the shareholders and the investing public.").

Plaintiffs rely on *Trautz v. Weisman*, 819 F.Supp. 282 (S.D.N.Y.1993), in which the residents of a facility for mentally ill adults alleged that a pattern of mail fraud involving misrepresentations made by the facility's owners to the New York State Department of Social Services ("DSS") proximately caused their injuries. Specifically, the defendants

misrepresented to DSS that the squalid conditions that existed at the facility would be corrected, when the real purpose of those assurances was to maintain the facility's operating certificate. Proximate cause for the RICO claim was satisfied, according to Judge Goettel, because the operating certificate, procured by fraud on the DSS, resulted in the residents' Supplemental Social Security Income ("SSI") benefits being higher, thereby allowing the defendants to charge the residents a higher monthly fee for substandard care. Judge Goettel concluded that "it was the residents ... who were intended to be the ultimate targets of defendants' alleged scheme. Fraudulently securing renewals of the operating certificate was only a necessary step in eventually parting the ... residents from their SSI monies." *Id.* at 287.

I respectfully disagree with Judge Goettel's decision in *Trautz*. He based it on a premise not justified by the proximate cause requirements of *Holmes* (which the *Trautz* opinion does not mention). Judge Goettel concluded that the plaintiff residents were the "alleged targets of the racketeering enterprise," *Trautz* at 287, ignoring the requirement that the "compensable injury necessarily is the harm caused by the predicate acts." *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 497, 105 S.Ct. 3275, 87 L.Ed.2d 346 (1985) (emphasis added). *See also Hecht*, 897 F.2d at 21 ("[T]he RICO pattern or [racketeering] acts must proximately cause plaintiff's injury."). In short, the conclusion in *Trautz* that injury by the "racketeering enterprise" is sufficient to confer RICO standing ignores the "direct-injury limitation" adopted by Congress

when it enacted 18 U.S.C. § 1964(c). *Holmes*, 503 U.S. at 272, 112 S.Ct. 1311.[6]

2. The 1962(b) Claim -

Even if plaintiffs had alleged injuries resulting directly from the racketeering acts, more would be required to sustain their 1962(b) claim. Essentially, that section prohibits racketeers from muscling in on enterprises. The RICO plaintiff must therefore allege a distinct injury caused by the defendants' acquisition or maintenance of an interest in or control of an enterprise. *See Discon, Inc. v. NYNEX Corp.*, 93 F.3d 1055, 1062-63 (2d Cir.1996). Here, the alleged enterprise is the association of the defendants themselves. *See* Complaint ¶ 61. They are alleged to have "maintained their interest in and control of said enterprise through a pattern of racketeering activity in violation of 18 U.S.C. § 1962(b)." Complaint ¶ 64.

First, the claim must fail because plaintiffs do not allege any facts to support a finding that the defendants' "interest" in their "association" was acquired or maintained through the pattern of racketeering activity. *See Discon*, 93

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[6] I assume, without deciding, that the reliance element of the plaintiffs' mail and wire fraud racketeering acts is established by HUD's reliance on the fraudulent statements. *See Cement and Concrete Workers Dist. Council Welfare Fund v. Lollo*, 148 F.3d 194, 196-97 (2d Cir.1998). The reliance element of a fraud claim is distinct from the proximate cause element of a civil RICO cause of action.

F.3d at 1062. Second, plaintiffs have failed to allege injury stemming from the defendants' acquisition or maintenance of that interest. *See id.* at 1063. Accordingly, the § 1962(b) claim must fail.

3. The 1962(d) Claims

Since I have held that the § 1962(b) and (c) claims do not state a cause of action, the RICO conspiracy claims, based solely on alleged agreements to commit the aforementioned acts, must be dismissed as well. *See Discon*, 93 F.3d at 1064.

C. The State Law Claim

Plaintiffs assert a state law claim seeking the appointment of an administrator to manage the Medgar Evers Houses. In light of the dismissal of the federal claims, it is appropriate to decline jurisdiction over these state claims. 28 U.S.C. § 1367(c)(3). *See also United Mine Workers v. Gibbs*, 383 U.S. 715, 726, 86 S.Ct. 1130, 16 L.Ed.2d 218 (1966) ("Certainly if the federal claims are dismissed before trial ... the state claims should be dismissed as well."); *Block v. First Blood Assocs.*, 988 F.2d 344, 351 (2d Cir.1993) (finding no abuse of discretion to dismiss state law discrimination claims where all federal claims had been dismissed before trial).

CONCLUSION

The plaintiff's allegations, which I accept as true, cry out for relief. There may well be an avenue for such relief in state court, as plaintiffs' counsel acknowledged during oral argument. For the reasons stated above, however, the civil

RICO cause of action is not a proper vehicle for these allegations.[7] The motion to dismiss is granted.

The Clerk of the Court is advised that this Order closes the case.

So Ordered.

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[7] Defendants raise various additional challenges to the RICO claims, which need not be addressed here.

UNITED STATES CODE ANNOTATED
TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I--CRIMES CHAPTER 96--RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS

Current through P.L. 106-55, approved 8-17-99

§1961. Definitions

As used in this chapter—

(1) "racketeering activity" means (A) any act or threat involving murder, kidnapping, gambling, arson, robbery, bribery, extortion, dealing in obscene matter, or dealing in a controlled substance or listed chemical (as defined in section 102 of the Controlled Substances Act), which is chargeable under State law and punishable by imprisonment for more than one year; (B) any act which is indictable under any of the following provisions of title 18, United States Code: Section 201 (relating to bribery), section 224 (relating to sports bribery), sections 471, 472, and 473 (relating to counterfeiting), section 659 (relating to theft from interstate shipment) if the act indictable under section 659 is felonious, section 664 (relating to embezzlement from pension and welfare funds), sections 891-894 (relating to extortionate credit transactions), section 1028 (relating to fraud and related activity in connection with identification documents), section 1029 (relating to fraud and related activity in connection with access devices), section 1084 (relating to the transmission of gambling information), section 1341 (relating to mail fraud), section 1343 (relating to wire fraud), section 1344 (relating to financial institution fraud), section 1425 (relating to the

procurement of citizenship or nationalization unlawfully), section 1426 (relating to the reproduction of naturalization or citizenship papers), section 1427 (relating to the sale of naturalization or citizenship papers), sections 1461-1465 (relating to obscene matter), section 1503 (relating to obstruction of justice), section 1510 (relating to obstruction of criminal investigations), section 1511 (relating to the obstruction of State or local law enforcement), section 1512 (relating to tampering with a witness, victim, or an informant), section 1513 (relating to retaliating against a witness, victim, or an informant), section 1542 (relating to false statement in application and use of passport), section 1543 (relating to forgery or false use of passport), section 1544 (relating to misuse of passport), section 1546 (relating to fraud and misuse of visas, permits, and other documents), sections 1581-1588 (relating to peonage and slavery), section 1951 (relating to interference with commerce, robbery, or extortion), section 1952 (relating to racketeering), section 1953 (relating to interstate transportation of wagering paraphernalia), section 1954 (relating to unlawful welfare fund payments), section 1955 (relating to the prohibition of illegal gambling businesses), section 1956 (relating to the laundering of monetary instruments), section 1957 (relating to engaging in monetary transactions in property derived from specified unlawful activity), section 1958 (relating to use of interstate commerce facilities in the commission of murder-for-hire), sections 2251, 2251A, 2252, and 2260 (relating to sexual exploitation of children), sections 2312 and 2313 (relating to interstate transportation of stolen motor vehicles), sections 2314 and 2315 (relating to interstate transportation of stolen property), section 2318 (relating to trafficking in counterfeit labels for phonorecords, computer

programs or computer program documentation or packaging and copies of motion pictures or other audiovisual works), section 2319 (relating to criminal infringement of a copyright), section 2319A (relating to unauthorized fixation of and trafficking in sound recordings and music videos of live musical performances), section 2320 (relating to trafficking in goods or services bearing counterfeit marks), section 2321 (relating to trafficking in certain motor vehicles or motor vehicle parts), sections 2341-2346 (relating to trafficking in contraband cigarettes), sections 2421-24 (relating to white slave traffic), (C) any act which is indictable under title 29, United States Code, section 186 (dealing with restrictions on payments and loans to labor organizations) or section 501(c) (relating to embezzlement from union funds), (D) any offense involving fraud connected with a case under title 11 (except a case under section 157 of this title), fraud in the sale of securities, or the felonious manufacture, importation, receiving, concealment, buying, selling, or otherwise dealing in a controlled substance or listed chemical (as defined in section 102 of the Controlled Substances Act), punishable under any law of the United States, (E) any act which is indictable under the Currency and Foreign Transactions Reporting Act, or (F) any act which is indictable under the Immigration and Nationality Act, section 274 (relating to bringing in and harboring certain aliens), section 277 (relating to aiding or assisting certain aliens to enter the United States), or section 278 (relating to importation of alien for immoral purpose) if the act indictable under such section of such Act was committed for the purpose of financial gain;

* * *

UNITED STATES CODE ANNOTATED
TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I--CRIMES

CHAPTER 96--RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS

Current through P.L. 106-55, approved 8-17-99

§1962. Prohibited activities

* * *

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

* * *

UNITED STATES CODE ANNOTATED
TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I--CRIMES
CHAPTER 96--RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS

Current through P.L. 106-73, approved 10-19-1999

§ 1964. Civil remedies

* * *

(c) Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee, except that no person may rely upon any conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of section 1962. The exception contained in the preceding sentence does not apply to an action against any person that is criminally convicted in connection with the fraud, in which case the statute of limitations shall start to run on the date on which the conviction becomes final.

* * *

UNITED STATES CODE ANNOTATED
TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I--CRIMES
CHAPTER 63--MAIL FRAUD

Current through P.L. 106-55, approved 8-17-99

§1341. Frauds and swindles

Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, or to sell, dispose of, loan, exchange, alter, give away, distribute, supply, or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, security, or other article, or anything represented to be or intimated or held out to be such counterfeit or spurious article, for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Postal Service, or deposits or causes to be deposited any matter or thing whatever to be sent or delivered by any private or commercial interstate carrier, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail or such carrier according to the direction thereon, or at the place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined under this title or imprisoned not more than five years, or both. If the violation affects a financial institution, such person shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.

UNITED STATES CODE ANNOTATED
TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I--CRIMES
CHAPTER 63--MAIL FRAUD

Current through P.L. 106-55, approved 8-17-99

§1343. Fraud by wire, radio, or television

Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined under this title or imprisoned not more than five years, or both. If the violation affects a financial institution, such person shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.

UNITED STATES CODE ANNOTATED
TITLE 42. THE PUBLIC HEALTH AND WELFARE
CHAPTER 8--LOW-INCOME HOUSING
SUBCHAPTER I--GENERAL PROGRAM OF ASSISTED HOUSING

Current through P.L. 106-55, approved 8-17-99

§1437f. Low-income housing assistance

(a) Authorization for assistance payments

For the purpose of aiding low-income families in obtaining a decent place to live and of promoting economically mixed housing, assistance payments may be made with respect to existing housing in accordance with the provisions of this section.

* * *

(c) Contents and purposes of contracts for assistance payments; amount and scope of monthly assistance payments

* * *

(4) The assistance contract shall provide that assistance payments may be made only with respect to a dwelling unit under lease for occupancy by a family determined to be a lower income family at the time it initially occupied such dwelling unit, except that such payments may be made with respect to unoccupied units for a period not exceeding sixty days (A) in the event that a family vacates a dwelling unit before the expiration date of the lease for occupancy or (B) where a good faith effort is being made to

fill an unoccupied unit, and, subject to the provisions of the following sentence, such payments may be made, in the case of a newly constructed or substantially rehabilitated project, after such sixty-day period in an amount equal to the debt service attributable to such an unoccupied dwelling unit for a period not to exceed one year, if a good faith effort is being made to fill the unit and the unit provides decent, safe, and sanitary housing. No such payment may be made after such sixty-day period if the Secretary determines that the dwelling unit is in a project which provides the owner with revenues exceeding the costs incurred by such owner with respect to such project.

* * *

CODE OF FEDERAL REGULATIONS
TITLE 24--HOUSING AND URBAN DEVELOPMENT
SUBTITLE B--REGULATIONS RELATING TO HOUSING AND URBAN DEVELOPMENT
CHAPTER VIII--OFFICE OF THE ASSISTANT SECRETARY FOR HOUSING-FEDERAL HOUSING COMMISSIONER, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT (SECTION 8 HOUSING ASSISTANCE PROGRAMS, SECTION 202 DIRECT LOAN PROGRAM, SECTION 202 SUPPORTIVE HOUSING FOR THE ELDERLY PROGRAM AND SECTION 811 SUPPORTIVE HOUSING FOR PERSONS WITH DISABILITIES PROGRAM)
PART 886--SECTION 8 HOUSING ASSISTANCE PAYMENTS PROGRAM--SPECIAL ALLOCATIONS
SUBPART A--ADDITIONAL ASSISTANCE PROGRAM FOR PROJECTS WITH HUD-INSURED AND HUD-HELD MORTGAGES
Current through January 1, 2000; 64 FR 73853

§ 886.108 Maximum annual contract commitment.

* * *

(c) Project Account. In order to assure that housing assistance payments will be increased on a timely basis to cover increases in Contract Rents or decreases in Family Incomes:

(1) A Project Account shall be established and maintained, in an amount as determined by the Secretary consistent with his responsibilities under Section 8(c)(6) of the Act, out of amounts by which the maximum annual Contract commitment per year exceeds amounts paid under

the Contract for any year. This account shall be established and maintained by HUD for each project as a specifically identified and segregated account, and payment shall be made therefrom only for the purposes of (i) housing assistance payments, and (ii) other costs specifically authorized or approved by the Secretary.

* * *

CODE OF FEDERAL REGULATIONS
TITLE 24--HOUSING AND URBAN DEVELOPMENT
SUBTITLE B--REGULATIONS RELATING TO HOUSING AND URBAN DEVELOPMENT
CHAPTER II--OFFICE OF ASSISTANT SECRETARY FOR HOUSING--FEDERAL HOUSING COMMISSIONER, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
SUBCHAPTER A--GENERAL
PART 200--INTRODUCTION TO FHA PROGRAMS
SUBPART H--PARTICIPATION AND COMPLIANCE REQUIREMENTS
PREVIOUS PARTICIPATION REVIEW AND CLEARANCE PROCEDURE
Current through January 1, 2000; 64 FR 73853

§ 200.219 Content of certification.

(a) Each principal who executes the certificate certifies that:

(1) The certificate contains a listing of every assisted or insured project of HUD, Farmers Home Administration and State or local government housing finance agencies in which the principal has been or is now a principal;

(2) For a period beginning 10 years prior to the date of the certificate under review and except as shown on the certificate;

(i) No mortgage on a project listed has ever been in default nor has mortgage relief been given;

(ii) There have been no defaults or noncompliances under any conventional construction contract or Turnkey contract of sale in connection with a public housing project;

(iii) There are no known unresolved findings raised as a result of HUD audits, management reviews or other governmental investigations;

(iv) There has been no suspension or termination of payments under any HUD assistance contract attributable to the fault or negligence of principal;

(v) The principal has not been convicted of a felony (See definitions § 200.215(b)) and is not presently the subject of a complaint or indictment charging a felony;

(vi) The principal has not been suspended, debarred, or otherwise restricted by any Department or Agency of the Federal Government or of a State Government from doing business with such Department or Agency;

(vii) The principal has not defaulted on an obligation covered by a surety or performance bond, and has not been the subject of a Claim under an employee fidelity bond;

(3) The principal has listed all parties who are known to him to be principals under § 200.215(e)(2);

(4) The principal is not a HUD employee or a member of an employee's immediate household as defined by HUD's Standards of Conduct in 24 CFR O.735-205(c);

(5) Except as shown on the certificate under review, the principal is not a participant (i) in a HUD assisted or insured project on which construction, as of the date of said certificate, has stopped for a period in excess of twenty days or; (ii) in an insured project on which construction, as of the date of said certificate, has been substantially completed for more than 90 days and documents for closing, including cost certification, have not been filed with HUD;

(b) The project owner shall certify that he has also listed all other parties who are principals under § 200.215(e)(1).

(c) If a principal cannot certify as to any items under paragraphs (a) and (b) of this section, such items may be deleted from the face of the certificate and a full explanation of the reason for the deletion, signed by the principal, may be attached to the certificate for HUD's review, evaluation and determination.

(d) Each principal who executes the certificate must also certify that said principal is not a Member of Congress or a Resident Commissioner.

CODE OF FEDERAL REGULATIONS
TITLE 24--HOUSING AND URBAN DEVELOPMENT
SUBTITLE B--REGULATIONS RELATING TO HOUSING AND URBAN DEVELOPMENT
CHAPTER II--OFFICE OF ASSISTANT SECRETARY FOR HOUSING--FEDERAL HOUSING COMMISSIONER, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
SUBCHAPTER B--MORTGAGE AND LOAN INSURANCE PROGRAMS UNDER NATIONAL HOUSING
ACT AND OTHER AUTHORITIES
PART 265--TRANSFER FROM NONPROFIT TO PROFIT-MOTIVATED OWNERSHIP FOR MULTIFAMILY HOUSING PROJECTS WITH HUD-INSURED OR HUD-HELD MORTGAGES
45 FR 54205, Aug. 14, 1980

§ 265.10 Criteria for approval.

(a) The proposed purchaser and its principals shall, to the Director's satisfaction, meet the following criteria as supported by written findings of fact:

* * *

(2) Show the ability to provide sound project management, especially sound physical and financial management. Employing a local management agent is strongly encouraged. If a proposed management agent is not local, the agent shall show evidence of its capacity to manage a project successfully outside the area of its principal place of business.

* * *

(4) Show an overall capacity, including financial capacity as determined by the Commissioner, to operate the project successfully for the remaining term of the mortgage. The involvement of the owner in other multifamily housing projects will be considered in making this determination.

* * *

OCCUPANCY REQUIREMENTS OF SUBSIDIZED MUTLI-FAMILY HOUSING PROGRAMS
Directive Number 43503 Chg. 15

CHAPTER 6. BILLING FOR ASSISTANCE PAYMENTS

SECTION 1. GENERAL INFORMATION

* * *

6-6. OWNER/AGENT MUST CERTIFY FORMS

A. Signing forms certifies:

- Assistance payments, recertifications, and special claims are computed accurately.
- All inspections have been completed i.e., move-in, move-out.
- Units are decent, safe, and sanitary.
- Assistance payments have not been billed or paid previously.
- Facts and data reported are actual and timely.
- Payments have not been received form the tenant or other sources beyond that authorized in the assistance contract or the lease, except as permitted by HUD.

NOTE: Owners/agents are not eligible for assistance payments until form HUD 50059 is signed by both owner/agent and tenant on or before the effective date of the form HUD 50059.

B. "Warning: 18 U.S.C. 1001 provides, among other things, that whoever knowingly and willingly makes or uses a document or writing containing any false, fictitious, or fraudulent statement or entry, in any matter within the jurisdiction of any department or agency of the United States, shall be fined not more than $10,000, or imprisoned for up to 5 years, or both".

C. Warning: 31 U.S.C. 3729 provides a civil penalty of not less than $5,000 and not more than $10,000, plus 3 times the amount of damages for any person who knowingly presents, or causes to be presented, a false or fraudulent claim; or who knowingly makes, uses, or causes to be used, a false record or statement; or conspires to defraud the Government by getting a false or fraudulent claim allowed or paid.

D. Owners/agents are also warned that false statements or false certifications may lead to the imposition of:

(1) Penalties and assessments under the Program Fraud Civil Remedies Act as implemented by HUD's Regulations, 24 CFR Part 30.

(2) Civil money penalties under the HUD Reform Act of 1989, as implemented by HUD's Regulations, 24 CFR Part 28.

(3) Administrative sanctions by HUD pursuant to CFR Part 24.

(2)

No. 99-1367

Supreme Court, U.S.
FILED
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CLERK

IN THE

Supreme Court of the United States

AMILIA ABBOTT, *et al.*,

Petitioners,

v.

MEDGAR EVERS HOUSES ASSOCIATES, L.P., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

In a civil action commenced under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 *et seq.* ("RICO"),

1. Has a fully developed divergence evolved among the Circuit Courts of Appeal as to whether a plaintiff must establish that it received and relied upon the fraudulent statements contained in the interstate mailings and wire communications which serve as predicate acts for a RICO claim?

2. Did the Court below ignore this Court's holding in *Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258 (1992), by adopting a "black-letter rule" that an injury to a plaintiff caused by misrepresentations to a third-party cannot serve as the basis for a cognizable RICO claim.

3. Did the Court below improperly append the element of justifiable reliance unto petitioners' RICO claim, thereby contradicting this Court's holding, in criminal mail and wire fraud proceedings, that "justifiable reliance . . . plainly [has] no place in the federal fraud statutes," in *Neder v. United States*, 527 U.S. 1 (1999).

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PRELIMINARY STATEMENT

Respondents respectfully submit this brief in opposition to the Petition for a Writ of *Certiorari* (the "Petition") to review the judgment of the United States Court of Appeals for the Second Circuit in the above-captioned case.

STATEMENT OF THE CASE

This action is symptomatic of the types of cases which have literally deluged the federal courts in recent years. Driven by the treble damage award provided by 18 U.S.C. § 1964(c), petitioners have sought to convert a prosaic landlord-tenant dispute into a "racketeering" action under the Racketeer Influenced and Corrupt Organizations Act ("RICO"). 18 U.S.C. § 1961, *et seq.* In essence, petitioners claim that Medgar Evers Houses Associates, L.P. ("MEHALP"), has not properly maintained Medgar Evers Houses, a low-income housing project, notwithstanding its receipt of rent subsidies from the Department of Housing and Urban Development ("HUD") pursuant to § 8 of the National Housing Act. 42 U.S.C. § 1441, *et seq.* Claiming that MEHALP fraudulently procured rent subsidy payments from HUD by misrepresenting the conditions at Medgar Evers Houses, petitioners have generally alleged that they "have suffered the substantial diminution in both the value of their occupancies as well as in the value of the millions of entitlement dollars paid to the owner on behalf of plaintiffs in the form of monthly rent subsidies." (Record 33, ¶ 77)[1] While petitioners' claims may be cognizable in state court, this landlord-tenant dispute hardly represents the type of "racketeering" activity which Congress intended to address when it enacted RICO.

---

1. References are to the Joint Appendix filed with the United States Court of Appeals for the Second Circuit. These references are designated as ("Record [page]).

A. The Complaint

Petitioners commenced this action on or about May 22, 1997. In substance, petitioners claim that Medgar Evers Houses is fraught with local housing code violations, and that MEHALP and its former and current managing agents, BPC Management and New England Management, respectively, have done little, if anything, to remedy these conditions. (Record 23-25, ¶¶ 34-35, 37-38). Certain MEHALP, BPC Management and New England Management principals were joined as defendants. HUD and the Department of Housing Preservation and Development of the City of New York were also named as nominal defendants. (Record 19, ¶¶ 15-16)

Alleging that the "racketeering enterprise" was an "associated in fact" enterprise comprised of MEHALP, BPC Management, New England Management and the individual respondents, petitioners claim that respondents engaged in a "pattern of three distinct types of mail and/or wire fraud." (Record 26, ¶ 45; 29, ¶ 61)[2] Significantly, the alleged predicate acts upon which petitioners' "pattern of racketeering activity" is predicated were all addressed to HUD, which was responsible for disbursing the § 8 rent subsidies directly to MEHALP.[3]

---

2. BPC Management and its former Vice President, Seymour Maslow, were named as defendants even though BPC Management had only managed Medgar Evers Houses "from in or about 1985 to in or about 1990." (Record 18-19, ¶¶ 11, 13). These claims were clearly barred by RICO's four-year statute of limitations. *See Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987); *Bingham v. Zolt*, 66 F.3d 553 (2d Cir. 1995), *cert. denied*, 517 U.S. 1134 (1996); *Bankers Trust Co. v. Rhoades*, 859 F.2d 1096 (2d Cir. 1988), *cert. denied*, 490 U.S. 1007 (1989).

3. Pursuant to the National Housing Act, HUD provides mortgage insurance and mortgages to the private sector at below-
(Cont'd)

First, in connection with the submission of monthly Owner's Certifications to HUD, petitioners claim that MEHALP committed "mail and/or wire fraud" by making "false and misleading" representations respecting the "safe, decent and sanitary condition of each unit." (Record 27, ¶ 49) The alleged fraud is not further particularized. Petitioners did not describe the substance of these alleged misrepresentations or the circumstances surrounding them in their Complaint. Rather, they asserted conclusorily that the "mail and/or wire fraud" was engaged in by "someone acting at . . . [MEHALP's] direction" over "each and every month since December 1985." (Record 27, ¶ 49) However, the Complaint charges that the alleged fraud was addressed to HUD, and that, relying upon these purportedly fraudulent representations, HUD disbursed the rent subsidy payments to MEHALP. (Record 27, ¶ 50)

The second type of "mail and/or wire fraud" allegedly "consist[ed] of a series of written statements transmitted to HUD in response to the findings of site inspection reports and management reviews conducted by HUD between 1986 and January 1997." (Record 27, ¶ 51) While petitioners identified six letters by date, they did not specify the alleged fraudulent representations or the circumstances surrounding their transmittal other than to assert that they "were intended to mislead HUD about the defendants' management capabilities, integrity, honesty and/or competence to implement improvements and reforms at the Project," and that these "letters . . . repeatedly assured HUD that major repairs and improvements were imminent when, in fact, no such major repairs were planned or implemented." (Record 27-28, ¶¶ 51-52, 54) Like the first type of purported "mail

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(Cont'd)
market rates for the development of low-income housing. HUD also disburses monthly rent subsidy payments to owners of qualified developments to the extent that a tenant's monthly contract rental charges exceed 30% of the tenant's adjusted gross income.

and/or wire fraud," this "series of written statements" was indisputably directed to HUD. Moreover, according to petitioners, these fraudulent missives were allegedly "intended to lull HUD into inaction and induce it to forego punitive and/or remedial enforcement actions against MEHALP or its managing agents . . ." (Record 28, ¶ 54)

The third type of alleged "mail and/or wire fraud" was also purportedly directed exclusively to HUD. These allegedly fraudulent communications consisted of "monthly and annual financial statements submitted to HUD by or on behalf of MEHALP . . . regarding the costs and expenses incurred in the management and operation of the Project." (Record 28, ¶¶ 55-56) Petitioners neither specified the nature of these fraudulent statements, the period over which the fraud occurred nor the circumstances surrounding these transmittals to HUD other than alleging generally that the "purpose of these material misrepresentations . . . [was] to conceal from HUD the 'diversion' and misappropriation of Project funds," and that these "diverted" funds "consisted of the rent paid directly by plaintiffs and the rent subsidy paid on their behalf . . ." (Record 28-29, ¶¶ 56-57)

The Complaint sought, *inter alia*, unspecified treble damages, the dissolution of the reputed racketeering enterprise, the "imposition of a trusteeship and/or receivership of said enterprise and all of its assets wherever situated," and an order directing respondents to divest themselves of any interest in the "enterprise" and Medgar Evers Houses. (Record 34-35, ¶ 83)

B. Procedural Background

Prior to the filing of respondents' motion to dismiss, the parties entered into two, Court-ordered stipulations. The first stipulation, dated June 11, 1997, provided for the Court's appointment of Jeffrey Goldstein, President of ARCO

Management Corporation ("ARCO"), as a Receiver to manage and operate Medgar Evers Houses pending the final disposition of the action. (Record 38-39) Pursuant to the second "Stipulation and Order," dated August 7, 1997, HUD became a mortgagee-in-possession of Medgar Evers Houses. While this order vacated the Goldstein receivership, the order provided that HUD would appoint Mr. Goldstein as its managing agent "to continue to manage and run the Medgar Evers Houses property." (Record 40-42)

On or about November 3, 1997, respondents moved to dismiss the Complaint. By Memorandum and Order, dated October 23, 1998, the District Court dismissed the Complaint. (Record 86-102) The Court held that petitioners' RICO claims could not be sustained because petitioners were not directly injured by respondents' alleged conduct, and, therefore, lacked standing to assert RICO claims.[4] Having dismissed petitioners' substantive RICO claims, the District Court also dismissed petitioners' § 1962(d) conspiracy claim and declined to exercise jurisdiction over petitioners' state law claim pursuant to *United Mine Workers v. Gibbs*, 383 U.S. 715, 726 (1966).[5]

In an unpublished opinion, the United States Court of Appeals for the Second Circuit summarily affirmed the dismissal of petitioners' Complaint. Consistent with this Court's opinion in *Holmes v. Securities Investor Protection*

4. The Court also held that petitioners' § 1962(b) claim could not be maintained because petitioners had (a) failed to allege facts from which the Court could infer that respondents had acquired or maintained an "interest" in their "association" through a pattern of racketeering activity and (b) neglected to allege any acquisition injury resulting from the enterprise.

5. Petitioners had asserted a claim pursuant to New York Real Property Actions and Proceedings Law §§ 769-778, seeking the appointment of an administrator to manage the Medgar Evers Houses.

Corp., 503 U.S. 258 (1992), the Court held that petitioners had not demonstrated the "loss causation necessary for RICO standing" because they had "failed to establish that the defendants' misrepresentations were the proximate source of the tenants' injuries." (Petition at 6a) Significantly, rather than than embracing the so-called "convergence theory" of RICO standing advanced by petitioners and holding that petitioners lacked standing because they had not reasonably relied upon the alleged misrepresentations addressed to HUD, the Second Circuit adhered to the proximate cause precepts delineated by this Court in *Holmes*, determining that petitioners had failed to allege that they were directly injured as a result of these alleged misrepresentations. As the Court, relying upon *Holmes* and its progeny, instructed:

> [T]o plead a direct injury is a key element for establishing proximate causation, independent and in addition to the other traditional elements of proximate cause. Thus, the other traditional rules requiring that defendant's acts were a substantial cause of the injury, and that plaintiff's injury was reasonably foreseeable, are additional elements, not substitutes for alleging (and ultimately showing) a direct injury [to petitioners]. (Petition at 6a)

REASONS FOR DENYING THE PETITION

I.

THIS CASE IS NOT RIPE FOR REVIEW BY THIS COURT BECAUSE NO DIVERGENCE OF OPINION HAS DEVELOPED AMONG THE CIRCUIT COURTS OF APPEAL RESPECTING WHETHER THE RICO PROXIMATE CAUSE STANDING REQUIREMENTS SHOULD BE RESTRICTED BY THE ADOPTION OF THE "CONVERGENCE THEORY" OF LIABILITY

A. Standard of Review

The considerations governing the issuance of a writ of *certiorari* are detailed in Rule 10 of this Court. U.S. Sup. Ct. Rule 10. Petitioners are not entitled to such a writ as a matter of right. Rather, this Court has discretion to grant such applications, and a petition for a writ of *certiorari* "will only be granted for compelling reasons." *Id.*; *Durham v. United States*, 401 U.S. 481 (1971); *Fay v. Noia*, 372 U.S. 391 (1963) (the grant of a writ of *certiorari* is a matter of sound judicial discretion, and will be granted only where there are important and special reasons for doing so).

While this Court will grant a petition for a writ of *certiorari* to resolve important conflicts among the U.S. Courts of Appeals, *Braxton v. United States*, 500 U.S. 344, 347 (1991), there must be a "clear conflict" among the appellate courts to warrant such review. *United States v. Dionisio*, 410 U.S. 1, 5 (1973). Moreover, a divergence of opinion among the federal appellate courts on a question of federal law, while an important consideration in assessing whether to grant a petition for a writ of *certiorari*, is not a conclusive factor. 23 Moore's Federal Practice § 510.21[1] at 510-14.

As one noted commentator observed,

> [t]he nub of all these qualifications is that a conflict of decisions may safely be relied on as a ground for certiorari only in instances where it is clear that the conflict is one that can be effectively resolved by the Supreme Court alone, and that the disagreement among the lower courts is one that should be dissolved.

23 Moore's Federal Practice § 510.21[2] at 510-16 (quoting Harlan, "Manning the Dikes," 13 Record of the N.Y.C. Bar Association 541, 552 (1958)). *See also* Frankfurter & Hart, "The Business of the Supreme Court at October Term 1933," 48 Harv. L. Rev. 238, 268-69 ("the Court is interested in conflicts which impair uniformity of decision as to matters of importance.")

B. There is No Clear Conflict Among the Circuit Courts Respecting the Application of the Convergence Theory of Liability

Petitioners' application for a writ of *certiorari* is predicated upon the erroneous theory that a clear divergence of opinion has developed among certain federal appellate courts respecting the application of the *Holmes* standing and injury requirements. Specifically, petitioners contend that, for purposes of applying proximate cause analysis, the Second and the Fourth Circuit Courts of Appeal have adopted the purported "convergence" theory of liability in civil RICO cases in which mail (18 U.S.C. § 1341) or wire fraud (18 U.S.C. § 1343) serve as the underlying predicate acts. In sum, this theory, as articulated by petitioners, would restrict RICO standing only to those parties who directly relied upon the underlying predicate fraudulent statements. Petitioners argue that, while the First, Third and Fifth Circuit Courts of Appeals have adopted a policy-based proximate cause

standard consistent with the dictates of *Holmes*, *United States v. Christopher*, 142 F.3d 46, 53 (1st Cir. 1998); *Tabas v. Tabas*, 47 F.3d 1280 (3d Cir. 1995); *In re Burzynski*, 989 F.2d 733 (5th Cir. 1993), the Second and the Fourth Circuit Courts of Appeals have abandoned these policy considerations and will only afford civil RICO standing to parties who have directly relied upon the alleged fraudulent predicate acts, *Medgar Evers Houses Tenants Association v. Medgar Evers Houses Associates, L.P.*, __ F.3d __ (2d Cir. 1999); *Brandenburg v. Seidel*, 859 F.2d 1179 (4th Cir. 1988), *rev'd on other grounds*, *Quackenbush v. Allstate Insurance Co.*, 517 U.S. 706 (1996). (Petition 8-11)

A careful review of the allegedly divergent opinions in the Second and Fourth Circuits, together with the wealth of authority addressing the RICO proximate causation requirement in the Second Circuit, establishes that there is no divergence of authority in RICO cases predicated upon mail or wire fraud which would warrant review by this Court. Prior to analyzing this authority, however, an analysis of this Court's opinion in *Holmes* is merited.

1. *The Holmes Decision*

In *Holmes*, the Securities Investor Protection Corporation ("SIPC"), a private nonprofit corporation established pursuant to federal statute to provide financial protection to customers of failed broker-dealers, asserted RICO claims against 75 defendants, alleging that they had engaged in a fraudulent scheme to manipulate the stock of six public companies and that this scheme resulted in the demise of two broker-dealers, including First State Securities Corporation ("FSSC"). Defendants were officers and directors of the six companies and former principals and employees of the broker-dealers. *See Securities Investor Protection Corp. v. Vigman*, 908 F.2d 1461, 1464 (9th Cir.

1990), *rev'd sub nom. Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258 (1992).

The SIPC charged that defendants had manipulated the stock of these companies by making unduly optimistic statements respecting the companies' prospects and sold small positions in these stocks on an ongoing basis to create the appearance of market liquidity. The broker-dealers, which had purchased substantial amounts of the stock for their proprietary accounts, experienced serious financial difficulties after the fraud was discovered and the stock prices plummeted. These broker-dealers were eventually liquidated, and the SIPC advanced nearly $13 million to the broker-dealers' customers to satisfy their claims. The SIPC asserted that defendant Holmes had issued false statements regarding the prospects of one of the six companies, Aero Systems, Inc., of which he was an officer, director and major shareholder, and that he had sold small amounts of one of the other company's stock to stimulate a market in its shares. *Holmes*, 503 U.S. at 263.

The SIPC, claimed that it was subrogated to the rights of those customers who, while they had neither purchased nor sold the manipulated securities, had nevertheless incurred losses as a result of the financial collapse of the broker-dealers.

In analyzing RICO's standing requirements, this Court, relying upon its previous interpretations of the Clayton and Sherman Act standing provisions from which 18 U.S.C. § 1964(c) was fashioned, held that a party had standing to assert RICO claims only if it could establish that its injuries were both actually and proximately caused by the alleged RICO predicate acts. This Court also emphasized that the "proximate cause" standard was a legal construct which implicated a number of jurisprudential policy concerns.

As this Court explained:

> Here we use "proximate cause" to label generically the judicial tool used to limit a person's responsibility for the consequences of that person's acts. At bottom, the notion of "proximate cause" reflects "ideas of what justice demands, or of what is administratively possible and convenient. W. Keeton, D. Dobbs, R. Keeton, & D. Owen, Prosser and Keeton on Law of Torts, § 41, p. 264 (5th ed. 1984). Accordingly, among the many shapes this concept took at common law, *see Associated General Contractors, supra*, 459 U.S., at 532-533, 103 S.Ct., at 905-906, was a demand for some direct relation between the injury asserted and the injurious conduct alleged. Thus, a person who complained of harm flowing merely from the misfortunes visited upon a third person by the defendant's acts was generally said to stand at too remote a distance to recover. *See, e.g.* 1 J. Sutherland, Law of Damages 55-56 (1882).

Id. at 268.

Those policy concerns, which this Court outlined in affirming the dismissal of the claims against Holmes relate to the jurisprudential impediments which the Courts would encounter by granting standing to too broad a spectrum of "injured" parties, and do not create a litmus test for the determination of civil RICO standing. As this Court generally cast this age-old conundrum:

> In a philosophical sense, the consequences of an act go forward to eternity, and the causes of an event go back to the dawn of human events, and beyond. But any attempt to impose responsibility

> upon such a basis would result in infinite liability for all wrongful acts, and would "set society on edge and fill the courts with endless litigation."

Id. at 266 n.10 (quoting W. Keeton, D. Dobbs, R. Keeton, & D. Owen, Prosser and Keeton on Law of Torts, § 41 at p. 264 (quoting *North v. Johnson*, 58 Minn. 242, 59 N.W. 1012 (1894)).

As this Court further explained, these jurisprudential considerations relate to the assessment and apportionment of damages, and the general impact which an unduly liberal standing rule would have upon the judicial system:

> Although such directness of relationship is not the sole requirement of Clayton Act causation, it has been one of its central elements, *Associated General Contractors*, 459 U.S., at 540, 103 S.Ct., at 909, for a variety of reasons. First, the less direct an injury is, the more difficult it becomes to ascertain the amount of a plaintiff's damages attributable to a violation, as distinct from other, independent factors. *Id.*, at 542-543, 103 S.Ct., at 910-911. Second, quite apart from problems of proving causation, recognizing claims of the indirectly injured would force courts to adopt complicated rules for apportioning damages among plaintiffs removed at different levels of injury from violative acts, to obviate the risk of multiple recoveries. *Id.*, at 543-544, 103 S.Ct. at 911-912; *Blue Shield of Virginia v. McCready*, 547 U.S. 465, 473-475, 102 S.Ct. 2540, 2545-2546, 73 L.Ed.2d 149 (1982); *Hawaii v. Standard Oil Co. Of Cal.*, 405 U.S. 251, 264, 92 S.Ct. 885, 892, 31 L.Ed.2d 184 (1972). And, finally, the need to grapple with these problems is simply unjustified by the general interest in deterring injurious

> conduct, since directly injured victims can generally be counted on to vindicate the law as private attorneys general without any of the problems attendant upon suits by plaintiffs injured more remotely. *Associated General Contractors, supra*, 459 U.S., at 541-542, 103 S.Ct., at 910-911.

Holmes, 503 U.S. at 269-70.

Considering the broad swarth which RICO could potentially cut across the jurisprudential landscape if its standing requirements are accorded too liberal an interpretation, these concerns applied with at least as much force in *Holmes*. Indeed, this Court, in affirming the dismissal of the claims against Holmes as "too remote," noted that, if it adopted the liberal standing rules being pressed by the SIPC, the salutary objectives of RICO would be irreparably compromised:

> [W]e fear that RICO's remedial purposes would more probably be hobbled rather than helped by SIPC's version of liberal constuction [of the standing requirements]: Allowing suits by those injured only indirectly would open the door to "massive and complex damages litigation [, which would] not only burde[n] the courts, but [would] also undermin[e] the effectiveness of treble damages suits." *Associated General Contractors*, 459 U.S., at 545, 103 S.Ct., at 912.

Id. at 274.

Thus, the standard articulated in *Holmes* is predicated upon the jurisprudential considerations which underlie traditional proximate cause analysis. While this Court, in *Holmes*, and other courts which have defined the universe of

potential claimants who have standing to sue for injuries which they have allegedly sustained have utilized judicial constructs such as the "directness" of the plaintiff's injuries and the "reasonable foreseeability" of those injuries, these concepts are merely terms utilized by the courts for determining, on a case-by-case basis, whether a party's injuries are cognizable at law. Indeed, the concept of "reasonable foreseeability" has served as the basis for "proximate cause" analysis since the New York Court of Appeals articulated the standard in *Palsgraf v. Long Island Railroad Co.*, 248 N.Y. 339, 162 N.E. 99 (1928), and is freighted with the same jurisprudential considerations outlined by this Court in *Holmes*.

2. *The Second Circuit Court of Appeals Has Not Adopted a "Reliance" Litmus Test in RICO Cases Predicated Upon Mail or Wire Fraud*

The Second Circuit Court of Appeals has not adopted a black letter "reliance" litmus test in RICO actions predicated upon mail or wire fraud, as argued by petitioners. Indeed, a review of the applicable authority in the Second Circuit only confirms that that Circuit has adhered to the flexible jurisprudential "proximate cause" standard articulated by this Court in *Holmes*.

For example, in *Sperber v. Boesky*, 849 F.2d 60 (2d Cir. 1988), the Second Circuit affirmed the dismissal of a RICO action commenced on behalf of investors who had purchased common stock or call options in six publicly-traded companies in which Ivan Boesky had an interest. In substance, the Complaint alleged that Boesky had engaged in securities fraud, commercial bribery, mail fraud and wire fraud, and that plaintiffs had been damaged when Boesky sold his stake in those companies without disclosing that he was about to plead guilty to securities fraud. Specifically, plaintiffs alleged that "[t]hey . . . [had] been damaged as a

result of their investment decisions to invest in takeover companies whose prices were artificially inflated as a result of the unlawful activities of [Boesky] and his reputation, falsely created and maintained." *Id.* at 62. Plaintiffs acknowledged that they had not been the direct targets of Boesky's alleged fraud. Nevertheless, they contended, like petitioners, that their "indirect" injuries were cognizable under RICO because these injuries were "reasonably foreseeable."

In dismissing this argument, the Second Circuit reiterated the jurisprudential considerations in which RICO "proximate cause" analysis is rooted:

> [W]e are usually skeptical of claims that a defendant is liable to hundreds of thousands or even millions of people, and the facts of this case do not require us to delineate the circumstances that would allow such a broad-ranging claim to stand. Plaintiffs were neither the targets of the racketeering enterprise nor the competitors nor the customers of the racketeer. Boesky did not cheat or deceive plaintiffs in any way with regard to the particular stocks in question since they did not know he had purchased them and he did not trade in them illegally. He did not corner the market or control the stocks in question. As noted above, *the doctrine of proximate cause reflects social policy decisions based on shared principals of justice*. Applying those principals, we conclude that Congress did not intend us to allow RICO recovery to plaintiffs with claims as attenuated as these.

Id. at 65 (emphasis supplied).

Similarly, in *In re American Express Shareholders Litigation*, 39 F.3d 395 (2d Cir. 1994), six American Express Company ("American Express") shareholders commenced a shareholder derivative action against certain present and former directors, officers and employees of American Express, claiming that defendants had violated RICO and their fiduciary duties to the shareholders by engaging in a defamatory campaign designed to compromise one of American Express's competitors. Plaintiffs alleged that American Express had incurred damages to "its business and property in that it has suffered the loss of substantial amounts in sales and profits, has been exposed to potential liability, [and] has incurred damage to its business and reputation" as a result of the failed campaign. *Id.* at 398.

In affirming the dismissal of plaintiffs' RICO claims, the Second Circuit explained that "the shareholders of American Express were not the intended targets of the RICO violations. Quite the contrary, the RICO violations were intended to benefit American Express by injuring one of its competitors . . . The injuries alleged thus were neither the 'preconceived purpose' nor the 'specifically intended consequence' of the defendants' act." *Id.* at 400. *Accord*, *Abrahams v. Young & Rubicam, Inc.*, 79 F.3d 234 (2d Cir.), *cert. denied*, __ U.S. __, 117 S. Ct. 66 (1996); *Hecht v. Commerce Clearing House, Inc.*, 897 F.2d 21, 23-4 (2d Cir. 1990); *Burdick v. American Express Co.*, 865 F.2d 527, 529 (2d Cir. 1989); *In re Crazy Eddie Securities Litigation*, 714 F. Supp. 1285 (E.D.N.Y. 1988) (Nickerson, J.).

Moreover, the Second Court, after noting that "*Holmes* essentially endorsed the definition of proximate cause that we had earlier adopted," analyzed the jurisprudential considerations which resulted in its determination that American Express had sustained neither "direct" nor "foreseeable" RICO injuries due to defendants' campaign against an American Express competitor:

> The normative considerations that informed the proximate cause analysis in *Holmes*, *Hecht* and *Sperber* weigh heavily in favor of not granting RICO standing to appellants. As in *Holmes*, the potential for duplicative recoveries created by granting standing to attenuated and indirect parties weighs against finding proximate causation. (Citation omitted) Such duplicative recoveries could well lead to, *inter alia*, superfluous deterrence. If appellants are correct that Freeman, Smith and Cantor [defendants] violated RICO by defaming Safra, then Safra, as the target and victim of the scheme, could sue Freeman, Smith and Cantor under RICO and recover treble damages for injuries to his business of property . . . such potential liability to the directly injured victim does create a significant deterrent to a RICO scheme.

American Express, 39 F.3d at 401.

In *Moore v. Painewebber, Inc.*, 189 F.2d 165 (2d Cir. 1999), the Court, in vacating the dismissal of a RICO claim which alleged that defendant had misrepresented a standard life insurance policy to be a form of individual retirement account, acknowledged that the Complaint properly averred that defendant had misrepresented the nature of the account and that plaintiffs had relied upon these representations. The Court, however, did not suggest that such reliance alone was sufficient to establish RICO standing. Indeed, the Court, citing *Holmes*, emphasized the traditional common law proximate causation requirements which the Congress adopted in enacting RICO:

> The inquiry into RICO's statutory purpose happens to lead back, at least in part, to the common law of proximate cause. Based upon an

> analysis of the statute's history, the Supreme Court has held that the language of 18 U.S.C. § 1964(c) reflects a congressional intent to require plaintiffs in civil actions under RICO to demonstrate not only but-for causation but also proximate causation as that concept is understood at common law.

Id. at 178.

The concepts of "foreseeability" and "direct injury" are, therefore, terms of art utilized in assessing whether a plaintiff's injuries are sufficiently proximate to warrant RICO standing. These concepts are rooted in the common law and represent flexible principles consistent with the jurisprudential considerations implicit in the doctrine of proximate causation.

The Second Circuit's decision in the case at bar does not represent a departure from these basic principles of proximate cause. The Court did not hold that petitioners had failed to state a RICO claim because petitioners had not relied upon respondents' alleged fraudulent misrepresentations. Rather, the Court, applying traditional proximate cause analysis, affirmed the dismissal petitioners' claims because petitioners' purported injuries could not be characterized as sufficiently direct to warrant RICO standing. As the Court observed:

> The tenants here failed to establish loss causation because they failed to establish that the defendants' misrepresentations were the proximate source of the tenants' injuries. "[T]o plead a direct injury is a key element of establishing proximate causation, independent of and in addition to the other traditional elements of proximate cause. Thus, the other traditional

> rules requiring that defendant's acts were a substantial cause of the injury, and that plaintiff's injury was reasonably foreseeable, are additional elements, not substitutes for alleging (and ultimately showing) a direct injury." *Laborers Local 17 Health & Benefit Fund v. Philip Morris, Inc.*, 191 F.3d 229, 235-36 (2d Cir. 1999).

(Petition at 6a)[6]

In sum, the Second Circuit Court of Appeals has consistently applied the traditional jurisprudential precepts outlined in *Holmes* for purposes of determining RICO standing. Whether the injury is characterized as "direct" or "foreseeable" is of no particular import. These are legal terms

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6. It should also be noted that, even if the Second Circuit decision in the case at bar could be construed as establishing a "reliance" proximate cause litmus test in RICO actions, the decision is an unpublished summary order which may not be cited as precedential authority. (Petition at 1a) Furthermore, even if this unpublished order diverged from the traditional proximate cause standards articulated by other Second Circuit panels, such "conflicts are better resolved by the court of appeals itself, sitting *en banc*." 23 Moore's Federal Practice § 510.21[2] at 510-15. *See Wisniewski v. United States*, 353 U.S. 901, 902 (1957) ("It is primarily the task of a Court of Appeals to reconcile its internal difficulties."). *See also* Harlan, *Manning the Dikes*, 13 Record of the N.Y.C. Bar Association 541, 552 ("[C]ontrary decisions between different panels of the same Court of Appeals will not be considered to present a reviewable conflict since such difficulties of views are deemed an intramural matter to be resolved by the Court of Appeals itself.").

Moreover, to the extent that petitioners contend that Supreme Court review is necessary to resolve purported conflicts among the district courts in the Second Circuit regarding the implementation of the "reliance" litmus test (Petition 13), it should be noted that such conflicts are also better left to the intermediary appellate courts rather than this Court. *See* 23 Moore's Federal Practice § 510.21[1] at 510-14.

utilized to state, in conclusory fashion, the courts' assessment that a RICO plaintiff's injuries are too attenuated to warrant RICO standing. Otherwise, the courts would be inundated with treble damage RICO suits which, like the case at bar, are no more than standard commercial disputes.

3. *The Fourth Circuit Court of Appeals Has Not Adopted a "Reliance" Litmus Test in RICO Cases Predicated Upon Mail or Wire Fraud*

Similarly, the Fourth Circuit Court of Appeals has not adopted a "reliance" litmus test for establishing proximate cause in RICO civil actions. Quoting selectively from *Brandenburg*, petitioners argue that the Fourth Circuit has held that "reliance is necessary to establish injury to business or property 'by reason of' a predicate act of mail fraud within the meaning of § 1964(c)." (Petition 10)

In fact, the Court, in *Brandenburg*, sustained the dismissal of a RICO complaint charging that the Maryland Savings-State Insurance Corporation ("MSSIC"), a quasi-public non-profit corporation had failed to properly regulate state-chartered savings and loan associations, resulting in substantial interest income losses to depositors. While the Court, in a footnote, did suggest that reliance was a necessary element for the establishment of RICO proximate causation (since the depositors had evidently not relied upon any misleading information disseminated by MSSIC), this footnote merely constituted dictum based upon no apparent authority. *Brandenburg*, 859 F.2d at 1187-88 n.10.

The Court ultimately affirmed the dismissal of the RICO claims against MSSIC based upon traditional proximate cause analysis:

> Causation principles generally applicable to tort liability must be considered applicable. These

> require not only cause-in-fact, but "legal" or "proximate" cause as well, the latter involving a policy determination: "whether the conduct has been so significant and important a cause that the defendant should be held responsible." [Citation omitted] As such, the legal cause determination is properly one of law for the court, taking into consideration such factors as the foreseeability of the particular injury, the intervention of other independent causes, and the factual directness of the causal connection.

Id. at 1189.

Indeed, the *Brandenburg* dictum was expressly rejected by the Fourth Circuit in *Mid Atlantic Telecom Inc. v. Long Distance Telephone Services, Inc.*, 18 F.3d 260 (4th Cir. 1994), in which the Court sustained a RICO complaint against the competitor of a reseller of long distance telephone services even though the allegedly injured reseller was *not* the immediate recipient of its competitor's fraudulent practices. With reference to the *Brandenburg* "reliance" dictum, the Court explained:

> We did not, however, intend to establish a rule that only injuries suffered by the immediate victim of a predicate act satisfied the "by reason of" requirement of § 1964(c). In conducting the traditional common-law proximate cause analysis, therefore, courts should focus on the temporal and circumstantial relationship between the defendant's conduct and the injury suffered by the plaintiff, and the foreseeability that intervening events would cause injury to the plaintiff . . . In *Brandenburg*, the causal connection was considered too tenuous, and plaintiff's theory ignored the more immediate causes of the injuries

> (*i.e.*, duplicity by the management of the savings and loans and failure of MSSIC to prevent those injuries.

Id. at 263.

Thus, it is evident that the purported conflict among the Circuit Courts of Appeals, as postulated by petitioners, does not, in fact, exist. None of the federal appellate courts which have considered the issue have restricted the *Holmes* proximate cause analysis such that only the immediate victim of the alleged predicate fraud is entitled to assert a RICO claim. Accordingly, there is no need for this Court to grant petitioners' application for a writ of *certiorari* since there is no clear divergence among the federal appellate courts with respect to the application of the *Holmes* proximate cause test.

II.

THE COURT BELOW DID NOT GRAFT A "RELIANCE" REQUIREMENT ON THE FEDERAL MAIL AND WIRE FRAUD STATUTES

In *Neder v. United States*, 527 U.S. 1, 119 S. Ct. 1827 (1999), this Court, in connection with its review of defendant's criminal mail and wire fraud convictions, observed that the "common-law requirements of 'justifiable reliance' and 'damages' . . . plainly have no place in federal fraud statutes." *Neder*, 119 S. Ct. at 1841. Petitioners contend that, by requiring that an injured party must demonstrate reasonable reliance upon the predicate misrepresentations in civil RICO actions based upon mail and wire fraud, the Court below improperly grafted a "reliance" element on the criminal mail and wire fraud statutes. This argument is clearly erroneous and does not deserve extended discussion. As detailed above, neither the Second Circuit nor any other federal appellate court has held that such reliance is necessary to establish RICO standing. Rather, traditional proximate

cause precepts govern the determination of whether a party has standing to assert RICO claims. These standards are governed by the jurisprudential considerations outlined in *Holmes*, which are typically determined based upon the "directness" and the "foreseeability" of the injuries.

This conclusion is confirmed by the Second Circuit's decision in *County of Suffolk v. Long Island Lighting Company*, 907 F.2d 1295 (2d Cir. 1989). In *Long Island Lighting*, utility ratepayers filed a RICO claim against Long Island Lighting ("LILCO"), claiming that LILCO's misrepresentations to the New York State Public Service Commission ("PSC") resulted in inappropriate rate increases. While the misrepresentations were made only to the PSC, and only the PSC could have relied upon the misrepresentations, the Court held that if LILCO's fraudulent statements had improperly caused rate increases, plaintiffs, although not the immediate targets of the fraud, would have standing to assert RICO claims because they would have been directly injured as a result of the fraud perpetrated upon LILCO.[7] *Id.* at 1311.

Thus, it is clear that the decision below, which was predicated upon the jurisprudential considerations implicit in the concept of proximate causation, neither established a restrictive black letter "reliance" standard in RICO actions predicated upon mail or wire fraud nor effected any modification of the statutory criminal mail and wire fraud statutes. Therefore, there is no basis for this Court to review that determination, as urged by petitioners.

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7. The Court concluded, however, that the evidence submitted at trial was insufficient to establish the necessary causal connection between LILCO's misrepresentations and the rate increases. *Id.* at 1311-12.

III.

THE SECOND CIRCUIT CORRECTLY AFFIRMED THE DISMISSAL OF PETITIONERS' RICO CLAIMS

The Court of Appeals correctly affirmed the dismissal of petitioners' RICO claims because any injuries allegedly sustained by petitioners, tenants in Medgar Evers Houses, as a result of misrepresentations purportedly made to HUD were much too attenuated to afford petitioners RICO standing. Indeed, the claimed injuries sustained by petitioners — the diminution of the value of their leasehold occupancies — only underscores the wisdom of the jurisprudential considerations articulated by this Court in *Holmes*. Significantly, petitioners do not claim that respondents failed to apply the HUD rent subsidies to their rental charges. Rather, they merely claim that respondents failed to properly maintain Medgar Evers Houses. How does one even begin to calculate the claimed diminution in the value of these tenants' leasehold occupancies? How are the alleged damages to be apportioned among the tenants of Medgar Evers Houses? Assuming that respondents misrepresented the condition of the housing project to HUD, HUD — and only HUD — sustained any direct injury because it would have been deprived of the rent subsidies under false pretenses and was in the optimum position to "vindicate the law as private attorneys general without any of the problems attendant upon suits by plaintiffs injured more remotely." *Holmes*, 503 U.S. at 269-70. *See Associated General Contractors of California, Inc. v. Carpenters*, 459 U.S. 519, 541-542 (1983).

With respect to the allegedly deteriorating condition of the housing project, we are confronted with what is essentially a landlord-tenant dispute which may be resolved by state courts which are designed to determine such disputes. The alleged damage to the "value of . . . [petitioners'

leasehold] occupancies" (Record 33, ¶ 77) cannot serve as the basis for federal RICO standing. Were that the case, the federal courts would literally be deluged with claimants asserting pedestrian state law claims (which would inevitably entail assertions of mail and wire fraud) in an effort to obtain the treble damage awards accorded by RICO.

In dismissing petitioners' claims, the District Court, concluded, like the Court of Appeals, that petitioners' alleged injuries were too indirect and attenuated to sustain RICO standing. In so doing, it clearly articulated the jurisprudential considerations which resulted in the dismissal of those claims:

> [The jurisprudential concerns expressed in *Holmes*] equally apply in this case . . . The second-level injuries plaintiffs claim to have suffered are analogous to those alleged by the SIPC in *Holmes* and would impose similar burdens on the courts. If this RICO claim proceeds, the fact-finder would be required to determine whether the complained of conditions at the Medgar Evers Houses in fact resulted from the false statements to HUD, as opposed to, for example, the defendants' poor management of the housing project. Putting that factual issue aside, permitting plaintiffs to maintain a treble damage action would seem to require the apportionment of possible recoveries among the directly defrauded (HUD) and others indirectly injured by the fraudulent scheme, a group not necessarily limited to plaintiff tenants. Finally, as in *Holmes*, the law need not shoulder these difficulties. HUD itself can deter fraudulent statements to HUD. Owners who make fraudulent statements face criminal prosecution under 18 U.S.C. § 1001, [Citation omitted], and remain

> subject to civil penalties and other remedies under the HUD regulations.

(Record 95-96)

Indeed, the decision below was entirely consistent with that reached in *Manson v. Stacescu*, 11 F.3d 1127 (2d Cir. 1993), a case which is directly analogous to this case. In *Manson*, two plaintiffs, one of which was an officer and fifty percent shareholder of Stavola-Manson Electrical Construction Company ("Stavola"), commenced a RICO action against 26 defendants, including Stavola's other fifty percent shareholder and a Stavola director, claiming that they comprised a RICO enterprise which "had looted the Company to the point of bankruptcy in order to enrich themselves." *Id.* at 1129.

Like petitioners, the *Manson* plaintiffs asserted that, as a result of defendants' illegal conduct, which allegedly included bribery, attempted extortion and mail fraud, the value of their interest in Stavola had declined appreciably. Like petitioners, the *Manson* plaintiffs asserted that they should be accorded RICO standing due to the nature of their relationship to defendants, contending that defendants had breached fiduciary duties to the shareholder plaintiffs. In rejecting these arguments, the Second Circuit held that neither the nature of the relationship between the parties nor the nature of the injuries allegedly incurred by plaintiffs could sustain a RICO claim since the injuries were derivative, rather than the direct result, of the predicate racketeering acts. Relying upon *Holmes*, the Court stated:

> The Mansons [plaintiffs] claim that David Manson has standing to sue as a fifty percent shareholder of the Company. A shareholder generally does not have standing to bring an individual action under RICO to redress injuries to the corporation in

> which he owns stock. *Rand v. Anaconda-Ericsson, Inc.*, 794 F.2d 843, 847 (2 Cir.), *cert. denied*, 479 U.S. 987, 107 S.Ct. 579, 93 L.Ed.2d 582 (1986). This is true even when the plaintiff is the sole shareholder of the injured corporation. *Sound Video Unlimited, Inc. v. Video Shack, Inc.*, 700 F.Supp. 127, 136 (S.D.N.Y. 1988). Since the shareholder's injury is not related directly to the defendant's injurious conduct.

Manson, 11 F.3d at 1131.

Reviewing the jurisprudential concerns at the heart of the *Holmes* decision, the Second Circuit concluded:

> These important policy concerns counsel strongly against a holding that would ease the requirements for standing under RICO. The Mansons essentially claim that the Company was looted, thereby causing the value of David Manson's shares to decline.

Id. at 1132.

While petitioners do not have an ownership interest in Medgar Evers Houses, they are effectively taking the same position as the Mansons. They claim that respondents have "looted" their § 8 subsidies, which they characterize as "entitlements," and have intentionally permitted the Medgar Evers Houses' infrastructure to deteriorate, thereby diminishing the "value of their occupancies." (Record 33, ¶ 77) Petitioners also contend that they should be accorded RICO standing because of the parties' landlord/tenant relationship, suggesting that they are "beneficiaries" of the § 8 subsidies. However, these perambulations only underscore the fact that there is no direct relationship between petitioners' alleged injuries and the allegedly fraudulent acts

addressed to HUD. Both *Holmes* and *Manson* instruct that such "indirect" injuries cannot convert this landlord/tenant dispute into a treble damage RICO action.

Ultimately, the question is where the courts should draw the RICO "standing" line. In *Holmes*, this Court instructed that, if a plaintiff could establish a *direct* relationship between its purported injuries and the predicate RICO acts, it could pursue a RICO claim. This standard represents the appropriate demarcation line, and was reiterated by the Second Circuit in this case. Should the courts cross that line and commence granting RICO standing to plaintiffs who have only been injured indirectly as a result of the activities of a reputed RICO enterprise, such a modification of the RICO standing requirements — one which is clearly being advanced by petitioners before this Court — would undermine the jurisprudential considerations inherent in the "proximate cause" precepts and convert a plethora of standard state law claims involving allegedly fraudulent statements, whether communicated by telephone or the mails — into federal racketeering claims. That was clearly neither the intent of the Congress when it enacted RICO nor the intent of this Court when it delineated the jurisprudential policy considerations underlying proximate causation for purposes of establishing RICO standing.

CONCLUSION

For all of the foregoing reasons, respondents respectfully request that this Honorable Court deny the petition for a writ of *certiorari*.

Respectfully submitted,

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(3)

Supreme Court, U.S.
FILED
MAY 4 - 2000
CLERK

No. 99-1367

IN THE

Supreme Court of the United States

AMILIA ABBOTT, *et al.*,

Petitioners,

v.

MEDGAR EVERS HOUSES ASSOCIATES, L.P., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONERS' REPLY BRIEF

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PRELIMINARY STATEMENT

Petitioners respectfully disagree with Respondents' statement that the instant case is no more than "a prosaic landlord-tenant dispute." On the contrary, the embezzlement of millions of dollars in federal rent subsidies and direct rent payments — funds which are statutorily and contractually mandated to provide these low-income tenant Petitioners with safe, decent and sanitary housing — cannot and should not be so disdainfully dismissed.[1]

Respondents' attempt to trivialize the nature of Petitioners' claims against them, in fact, seeks merely to divert attention from the consequences of their decade of racketeering and immunize Respondents from the civil relief accorded by 18 U.S.C.§1961, *et seq.*

POINT I: RESPONDENTS MISSTATE THE HOLDING OF THE COURT BELOW

In a strange turnabout from their position below, Respondents no longer assert that, in order to satisfy the direct injury component of RICO causation, the party deceived by the predicate acts must be the same as the party injured by them (i.e., "convergence theory"). Instead, they now claim that convergence theory is neither the law nor the holding of

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[1] The statement in Respondents' Brief, at page 1, that this action is "symptomatic of the types of cases that have deluged the federal courts in recent years", is not only entirely outside the record; there is absolutely no evidence of its truth. If, in fact, there has been such a deluge, it is far more likely to originate with the financial and business sectors and to involve commercial disputes, rather than actions by discrete low-income groups such as Petitioners.

the Court below. Respondents' Brief, at pp. 8-9. Respondents' argument not only contradicts their earlier position; it flatly misstates the decision of the Court below. Although Respondents cite selected portions of the decision below, conspicuously absent is the clear, unambiguous language embracing "convergence theory." Specifically, the Court below held:

> As the district court concluded, the tenants *can allege no direct injury because the defendants' misrepresentations were made only to HUD.* The tenants' injuries are therefore *necessarily derivative of injuries sustained by HUD.* Because such derivative injuries are insufficient to establish proximate cause . . . *the tenants cannot establish the loss causation necessary for RICO standing.*

(App. at 6a) (Emphasis added).[2]

This holding, that Petitioners are categorically excluded as a matter of law from establishing direct injury because the fraudulent mailings were transmitted to HUD, rather than to them, is a clear and unambiguous adoption of convergence theory. Thus, the conflict between the Second Circuit Court of Appeals and the Courts of Appeal for the First, Third and Fifth Circuits is clear.

Not only have Respondents reversed their position as to convergence theory; they also seem to agree with Petitioners that there should not be any "reliance" requirement

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[2] References are to the Appendix annexed to Petitioners' Petition for a Writ of Certiorari. These references are designated (App. at [page]).

imported into the mail and wire fraud statutes. But they again misstate the holding of the Court below by claiming that it does not, in fact, require reliance on the misrepresentations that constitute the acts of mail fraud. Respondents' Brief at 14.

In arguing that such "reliance" was not required by the Court below, Respondents again manage to omit any reference to the plain language of the decision:

> The causation requirement, which is jurisdictionally mandated, has two different components. There must be 'transaction causation', *meaning that the misrepresentation must have led the plaintiffs to enter into the transactions at issue. . . .*

(App. at 6a, citing *Moore v. Paine Webber, Inc.*, 189 F. 3d 165, 169-70 (2d Cir. 1999)) (Emphasis added).

Respondents fail to explain how acts of mail fraud could possibly "have led the plaintiffs to enter into the transactions at issue . . ." *unless* the plaintiffs were aware of and had acted in reliance upon them. Thus, not only does this case establish the clear conflict between the Second Circuit and the First, Third and Fifth Circuits on this issue of judicially importing a reliance element into the mail and wire fraud statutes, that conflict is also established by the decision in *Moore v. Paine Webber, Inc., supra*, which the decision below invokes.

Moreover, it is evident that the case-by-case, common law proximate cause inquiry set forth in *Holmes v. Security*

Investor Protection Corp., 503 U.S. 258 (1992), and cited by Respondents, was precluded in this case by:

- the legal conclusion of the Court below that the mere *divergence* of identity alone between the party deceived by the mailed misrepresentations and the party injured rendered it *necessarily* impossible for Petitioners to establish "loss causation"; and

- the legal conclusion of the Court below that "transaction causation" cannot be factually established by any means other than showing that the mailed or wired misrepresentations *themselves* led the Petitioners into the transactions at issue.

In attempting to conceal the conflicts between the Circuit Courts of Appeal on the "reliance" issue, Respondents also contend that the Fourth Circuit Court of Appeals has retreated from its decision in *Brandenburg v. Seidel*, 859 F.2d 1179, 1187-88 n.10 (4th Cir. 1988), which held that "reliance is necessary to establish injury to business or property 'by reason of' a predicate act of mail fraud . . . ." Respondents' Brief at pages 20-21. In truth, the case which Respondents cite, *Mid-Atlantic Telecom, Inc. v. Long Distance Services*, 18 F.3d 260, 263 (4th Cir. 1994), while it questions the holding in *Brandenburg*, does not overrule it. Moreover, even if *Mid-Atlantic Telecom*, did overrule the reliance language of *Brandenburg*, this would simply mean that the Second Circuit Court of Appeals was in conflict with *four* other circuits rather than three.

Further, in an effort to portray the Second Circuit as in accord with the other circuits on the reliance issue, Respondents cite *County of Suffolk v. Long Island Lighting Company*, 907 F.2d 1295 (2d Cir. 1989), for the proposition that the Second Circuit has *not* held that such reliance is necessary to establish RICO standing. Respondents' Brief at 22. Ironically, this was exactly the position taken by the Petitioners in both the District Court and the Second Circuit Court of Appeals, that was rejected by both Courts. Indeed, in rendering their decisions, neither Court even mentions *County of Suffolk* despite the fact that this Court relied on it in *Holmes*. *Holmes*, 503 U.S. at 274 n. 19.

On the contrary, the District Court below expressly assumed that there *was* such a reliance requirement, holding "I assume, without deciding, *that the reliance element of the plaintiffs' mail and wire fraud racketeering acts* is established by HUD's reliance on the fraudulent statements." (App. at 25a, n.6) (Emphasis added). The Second Circuit decision in this case thus effectively affirms the requirement of reliance on the misrepresentations or mail and wire frauds as an element of "transaction causation." (App. at 6a).

POINT II: RESPONDENTS' CONTENTION THAT PETITIONERS' INJURIES WERE ATTENUATED AND INDIRECT, AND THAT HUD WAS THE ONLY DIRECTLY INJURED PARTY, IS ERRONEOUS AS A MATTER OF FACT AND LAW

Respondents assert that "Assuming that respondents misrepresented the condition of the housing project to HUD, HUD — and only HUD — sustained any direct injury *because*

it would have been deprived of the rent subsidies under false pretenses and was in the optimum position to 'vindicate the law as a private attorneys general without any of the problems attendant upon suits by plaintiffs injured more remotely.'"[3] Respondents' Brief at 24 (citing *Holmes, supra)* (Emphasis added).

This assertion misstates HUD's relationship to the stolen monies, ignores Petitioners' relationship to those funds, and incompletely describes the acts of mail fraud. Specifically, their assumption that HUD "owned " the rent subsidy money paid to Respondents each month is wrong as a matter of law.[4] On the contrary, the monies used by HUD to pay the rent subsidies, rather than being *owned* by HUD, were appropriated and earmarked by Congress to fund the specific Housing Assistance Payment contract of which these Petitioners were the third party beneficiaries. (App. at 35a-36a; *see also*, Petition for a Writ of Certiorari at 17-20).

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[3] Respondents misrepresented far more than the *condition* of the housing project. They also deceived HUD for a decade as to their criminal diversion of project repair and maintenance funds and misled HUD as to Respondents' purported plans to repair and improve hundreds of building code violations.

[4] Respondents also fail to explain how HUD — a federal agency — would be in the optimum position to act as a *private* attorney general. If, by that, Respondents mean that the federal subsidy money that they embezzled could be recovered *by HUD*, then they are incorrect as a matter of law because all moneys recovered in such a lawsuit would go to the United States Treasury, not to the agency. Moreover, this recovery would in no way redress the diminution in the value of petitioners' leaseholds, directly caused by Respondents' fraudulent scheme.

Respondents further claim that Petitioners ". . . merely claim that Respondents failed to properly maintain Medgar Evers Houses." Respondents' Brief at 24. This statement mischaracterizes the Complaint, implying that Petitioners merely alleged incompetent or negligent management on the part of the Respondents, as if that were an independent, intervening factor in the catastrophic deterioration of the project.

The Petitioners' actual complaint, of course, is that Respondents stole a substantial portion of the money paid to Respondents by HUD *and* the tenants, mandated for operating, repairing and maintaining the premises, and kept that money for themselves. Respondents successfully engaged in this fraudulent scheme for more than a decade by lying to HUD not only about the actual conditions of the Project and their promises to make improvements, but also about how these commingled rent monies were being used. The foreseeable and inevitable damage to the value of Petitioners' leaseholds — which flowed from a looting scheme largely implemented through acts of mail and wire fraud — is in no way attenuated or remote from either Respondents, with whom Petitioners were in direct and third party privity, or their acts, which were designed to and did loot the Project account containing the operation and maintenance monies for Petitioners' apartments.

Where Congress imposes on a federal agency the duty to oversee and regulate the conduct of certain persons, businesses and enterprises in order to protect specific classes of private citizens, and to assure that those citizens are not deprived of specific benefits conferred on them by law, it effectively makes that agency responsible for securing the rights and benefits of such classes of people. When the

discharge of that duty is obstructed and prevented by a pattern of deceptions and misrepresentations on which the agency relies, and, as a result, the benefits intended for the class of private citizens are diverted to the benefit of the deceivers, *it is the private citizens who are directly and proximately injured in their property.*

Because the decision of the Court below stands for the opposite proposition, that as a matter of law, such private citizens cannot have been proximately injured, and because the decision below is in conflict with the Courts of Appeal for the First, Third and Fifth Circuits, it should be reviewed and overturned by this Court.

CONCLUSION

For all of the foregoing reasons expressed herein and in the Petition for a Writ of Certiorari, Petitioners respectfully request that this Honorable Court grant the Petition for a Writ of Certiorari.

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